IN THE

Supreme Court of the United States

OCTOBER TERM, 1968

No. 473

JOHN H. BINGLER, District Director of Internal Revenue, PETITIONER

vs.

RICHARD E. JOHNSON, et al.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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CIVIL DOCKET

UNITED STATES DISTRICT COURT FOR THE
WESTERN DISTRICT OF PENNSYLVANIA

Judge Marsh JURY

Jury demand date:

RICHARD E. JOHNSON and BEVERLY P. JOHNSON, his wife, and MARTIN L. POMERANTZ and PHYLLIS L. POMERANTZ, his wife, and RICHARD A. WOLFE and ANNE F. WOLFE, his wife

v.

JOHN H. BINGLER, Dist. Director of Int. Rev.

ATTORNEYS

For plaintiff:
Dougherty, Larrimer & Lee
901 Grant Bldg. (19)

For defendant:
U. S. Attorney
633 U. S. Post Office &
Court House (19)

Docket Entries

1965

Sept. 22—Complaint filed.

Sept. 22—Summons issued.

Oct. 25—Summons returned served 10-19-65 on Dist. Director of Int. Rev. & U.S. Atty.; served on Atty. Gen. by certified mail, return receipt dated 10-13-65.

Dec. 3—Amended Complaint filed by pltfs. with Order entered allowing same to be filed and amending caption. (Marsh, J.)

Dec. 13—Answer to pltfs' Amendment to Complaint filed.

Dec. 15—Answer filed by deft. on 12/3/65 and Order dated 12/15/65 entered thereon granting leave to file same as of 12/3/65. (Marsh, J.)

Dec. 15—Order entered fixing pretrial procedure. (Marsh, J.)

1966

Jan. 7—Notice of taking the depositions of Richard E. Johnson, Martin L. Pomerantz and Richard A. Wolfe, filed by deft.

Feb. 14—Pretrial Statement filed by pltfs.

Feb. 17—Depositions of Richard E. Johnson, Martin L. Pomerantz and Richard A. Wolfe filed.

Feb. 21—Deft's pre-trial stmt filed.

Mar. 25—Pretrial Stipulation of counsel filed.

April 20—Deft's. requested special interrogatories filed and deft's. Alternative Requested Special Interrogatories filed.

April 20—Deft's. requested Instructions to the Jury filed by deft.

April 25—Motion filed by deft. and Order entered directing that the pretrial conference scheduled for 4-26-66 at 2:30 P.M. is hereby continued to a date of which counsel will be notified by the Court. (Marsh, J.)

Sept. 14—Transcript re: pretrial conference held 9/13/66 before Marsh, J. filed. (Rep. Blaney Cook)

Sept. 14—Pretrial held 9/13/66 before Marsh, J. and concluded. Hearing memo filed. (Rep. Blaney Cook)

Sept. 14—Pretrial order dated 9/13/66; case assigned to Master list for trial by Marsh, J. (Marsh, J.)

Nov. 18—Deft's list of exhibits filed.

Nov. 18—Deft's final listing of witnesses and exhibits filed.

Nov. 21—Stipulation in re number of jurors filed.

Nov. 21—Trial opens before Marsh, J. and a Jury.

Nov. 22—Trial continues.

Nov. 23—Trial continues.

Nov. 28—Trial continues. and concludes. Trial memo filed. (Rep. B. Cook)

Nov. 28—Verdict answered by the jury and filed. Verdict sheet filed. (in favor of deft) (Mr. Michael Arkin, Esq. counsel for deft. to make up judgment-from Washington)

Nov. 28—Order re meal and hotel accommodations for jurors filed. (Marsh, J.)

Nov. 29—Pltf's points for charge filed.

Nov. 29—Pltf's additional request for charge filed.

Dec. 2—Judgment order entered by the court in favor of deft., together with costs, and dismissing complaint with prejudice (Marsh, J.)

Dec. 5—Pursuant to Judgment order entered, judgment is hereby entered in favor of deft, and against pltf., together with costs, and complaint is hereby dismissed with prejudice. James H. Wallace, Jr., Clerk

Dec. 5—Notice mailed.

Dec. 2—Motion for New Trial filed by pltfs.

Dec. 6—Order entered directing that movants file brief on or before 2-3-67 & respondent shall file brief on or before 2-13-67 & further ordered that argument on motion for new trial is fixed for 2-16-67 at 3:00 P.M. Unless specifically requested in writing, no court reporter shall be present at this argument. (Marsh, J.)

Dec. 6—Bill of costs in the amount of $43.28 filed by U. S. (deft.)

1967

Jan. 5—Letters mailed counsel of record advising that costs will be taxed by the Clerk 1/11/67.

Jan. 9—Transcript filed re: Jury trial held at Pgh. commencing 11-21-66 before Marsh, J. and a Jury. (Rep. B. Cook) (Volume 3, Judge's Charge on 11-28-66)

Jan. 11—Costs in the amount of $43.28 taxed by the Clerk against the pltf. James H. Wallace, Jr. Clerk

Jan. 27—Satisfaction of Judgment filed by U.S.A.

Jan. 27—Pursuant to Satisfaction filed, Judgment entered in above entitled action is hereby marked satisfied.
James H. Wallace, Jr., Clerk

Feb. 16—Hearing on Motion for New Trial begun and concluded C.A.V. before Marsh, J. Hearing memo filed. (Rep. none)

March 6—Transcript of trial held before Marsh, J. (Rep: B. Cook) (Vol. 1)

March 6—Transcript of trial held before Marsh, J. (Rep: B. Cook) (Vol. 2)

July 3—Opinion filed and Order entered directing that the pltfs' motion for a new trial is denied. (Marsh, J.)

July 26—Notice of Appeal filed by pltfs.

July 26—Copy of Notice of Appeal mailed U. S. Court of Appeals; letters to counsel of record and Judges Marsh and Gourley. (Pltfs served U. S. Atty. with a copy)

Aug. 1—Bond for Costs on Appeal in the amt of $250.00 posted by plts. (Surety-Golen Falls Ins. Co.)

[1] IN THE UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF PENNSYLVANIA

CIVIL ACTION 65-1033

RICHARD E. JOHNSON and BEVERLY JOHNSON, his wife, and MARTIN L. POMERANTZ and PHYLISS POMERANTZ, his wife, and RICHARD A. WOLFE and ANNE F. WOLFE, his wife, *Plaintiffs:*

v.

JOHN H. BINGLER, District Director of Internal Revenue, *Defendant:*

Transcript of Proceedings

Civil Jury Trial, U. S. District Court, Pittsburgh, Pa., Commencing November 21, 1966.

BEFORE: HON RABE F. MARSH, U. S. District Judge, and a jury.

• • •

[2] INDEX

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Richard E. Johnson	75	112	128	
Dr. Gerald T. Horne	130	148	155	
Richard A. Wolfe	157	167	174	

[3] PROCEEDINGS

Monday Morning,
November 21, 1966.

(A jury of twelve members was duly empaneled.)

* * *

[14]

* * *

Mr. Larrimer: Your Honor, I might say for the record at this time that I have no objection to that as an accurate statement of the regulations as they exist. As a matter of a charge to the jury, I would take exception to any portion of that relating to compensation for services performed, either past, present or future, unless there is produced at the trial evidence of those facts to which that portion of the charge could relate.

The Court: Do you expect to produce evidence to that effect?

Mr. Arkin: Yes, Your Honor, I do.

The Court: I was sure he did. He equates these scholarships with compensation to Westinghouse. I don't know whether it is past, present or future, or all three of them.

Mr. Arkin: Neither do I.

The Court: Nobody knows, but that great jury will be able to determine that for us.

* * *

[28] The Court:

* * *

It is stipulated between the parties that this is a civil action for the refund of income taxes alleged to have been erroneously assessed and collected on behalf of the following named taxpayers for the taxable years indicated, and in the following amounts, plus interest according to law.

The Plaintiff Richard E. Johnson and Beverly P. Johnson, amount $395 for the year 1960 and $599.82 for the year 1961.

Martin L. Pomerantz and Phyllis L. Pomerantz,
[29] the amount $276.68 for the year 1961 and $312.10 for the year 1962.

Richard A. Wolfe and Anne F. Wolfe, $985.31 for the year 1960 and $362.24 for the year 1961.

It was further stipulated by the parties that the Plaintiffs Johnson—Mr. and Mrs. Johnson—timely filed joint income tax returns for the years 1960 and 1961.

The Plaintiffs Johnson filed amended tax returns on April 4, 1963 seeking refunds of $395 for 1960 and $599.82 for 1961.

On September 27, 1963, the District Director of Internal Revenue issued statutory notices of disallowance denying the Plaintiffs' claims for refund.

The Plaintiffs Pomerantz timely filed joint income tax returns for the years 1961 and 1962.

The Plaintiffs Pomerantz filed amended tax returns seeking refunds of $276.68 for 1961 and $312.10 for 1962.

On March 29, 1965 the District Director of Internal Revenue issued statutory notices of disallowance denying Plaintiffs' claims for refund.

This suit—the one you are trying—was filed on September 22, 1965, I believe, on behalf of Johnson and Pomerantz.

The Plaintiffs Wolfe timely filed joint income
[30] tax returns for the years 1960 and 1961. The Plaintiffs Wolfe filed amended tax returns on April 24, 1963 seeking refunds of $985.31 for 1960 and $362.24 for 1961.

On December 20, 1963, the District Director of Internal Revenue issued statutory notices of disallowance denying Plaintiffs' claims for refund.

The Plaintiffs Wolfe were made parties Plaintiff in this action which you are trying by an amended complaint filed in this court on December 3, 1965.

It was further stipulated by the parties that the Plaintiff Beverly F. Johnson is named as a Plaintiff only because there was a joint income tax return for the years involved. As you will recall, Beverly is Mr. Johnson's wife.

Richard E. Johnson has been employed by Westinghouse Electric Corporation since 1956. Richard E. Johnson was granted an educational leave for a period of nine months from October 1, 1960 to June 30, 1961.

Richard E. Johnson obtained a Doctor of Philosophy degree, commonly called a PhD degree, in metallurgical engineering from Carnegie Institute of Technology in 1965.

The educational leave was taken pursuant to the Westinghouse Bettis Fellowship and Doctoral Program.

While on educational leave, Westinghouse paid Richard E. Johnson $1,890 in 1960 and $3,780 in 1961.

[31] It was further stipulated and agreed by the parties that the Plaintiff Phyllis L. Pomerantz is named as a Plaintiff only because there was a joint income tax return filed for the years involved. Phyllis Pomerantz is the wife of Mr. Martin Pomerantz.

Martin L. Pomerantz has been employed by Westinghouse Electric Corporation since 1957. Martin L. Pomerantz was granted an educational leave for a period of nine months from November 1, 1961 to July 31, 1962.

Martin L. Pomerantz obtained a Doctor of Philosophy degree in Mechanical Engineering from the University of Pittsburgh in 1962. The educational leave was taken pursuant to the Westinghouse Bettis Fellowship and Doctoral Program.

While on educational leave, Westinghouse paid Martin L. Pomerantz $1,260 in 1961 and $4,410 in 1962.

It was further stipulated and agreed by the parties that the Plaintiff Anne F. Wolfe is named as a Plaintiff only because there was a joint income tax return filed for the years involved. Anne Wolfe is the wife of Richard Wolfe.

Richard A. Wolfe was employed by Westinghouse Electric Corporation in 1952. Richard A. Wolfe was granted an educational leave for a period of twelve months from March 1, 1960 to February 28, 1961.

[32] Richard A. Wolfe obtained a Doctor of Philosophy degree in Mechanical Engineering from Carnegie Institute of Technology in 1963. The educational leave was taken pursuant to the Westinghouse Bettis Fellowship and Doctoral Program.

While on educational leave, Westinghouse paid Richard A. Wolfe $8,052.40 in 1960 and $1,646.50 in 1961.

It was further stipulated and agreed by the parties as follows. Doctor Johnson—that is Richard E. Johnson—signed an employment agreement by which he agreed that at the end of the educational leave he would assume such duties commensurate with his education and experience as may be assigned to him by Westinghouse, and that he would thereafter continue in the employ of Westinghouse

for at least two calendar years from the date he assumed those duties, and at a rate of salary commensurate with the duties assigned.

Doctor Pomerantz—that is Martin L. Pomerantz—signed an employment agreement by which he agreed that at the end of the educational leave he would assume such duties commensurate with his education and experience as may be assigned to him by Westinghouse, and that he would thereafter continue in the employ of Westinghouse for at least two calendar years from the date he assumed those duties, and at a rate of salary commensurate with the duties assigned.

Doctor Wolfe—that is Richard A. Wolfe—did not sign such a written agreement, but he was informed by Westinghouse that he was expected to return to the
[33] employ of Westinghouse for a period at least equivalent to his period of educational leave.

It was further stipulated and agreed by the parties that the Bettis Fellowship and Doctoral Programs are available only to selected employees of the Bettis Atomic Power Laboratory of the Westinghouse Electric Corporation.

Participants in the program may elect to pursue the degree of Doctor of Philosophy in the field of mechanical, electrical, chemical or metallurgical engineering, or physics or mathematics, at either the University of Pittsburgh or the Carnegie Institute of Technology.

In obtaining the Doctor of Philosophy degree under this program, the participants must satisfy the requirements of the University of Pittsburgh or the Carnegie Institute of Technology for the granting of such degree in the same manner as other candidates for that degree.

The Carnegie Institute of Technology and the University of Pittsburgh are educational institutions as defined by a certain section of the Internal Revenue Code of 1954.

• • •

[34] MARTIN L. POMERANTZ,

called as a witness in behalf of the Plaintiffs and being duly sworn, testified as follows:

Direct Examination

By Mr. Larrimer:

Q. You are one of the Plaintiffs in this case, Mr. Pomerantz? A. Yes, I am.

Q. Where do you live now? A. 5147 Leona Drive, Pittsburgh, Pennsylvania.

Q. Do you have a family? A. Yes, I do.

Q. How many children? A. Three children.

Q. What is your present employment? A. I am a consulting engineer in private practice.

Q. How long have you been in private practice? A. For fourteen months.

Q. What is your beginning date of employment at Westinghouse? When did you start at Westinghouse? A. July 1957.

Q. Had you been employed prior to this time? A. A summer job in 1956 with the Bethlehem Steel Company for one month.

[35] Q. And, what was your education, Mr. Pomerantz, prior to your employment with Westinghouse in 1957? A. I had a Master's degree in Mechanical Engineering and a Bachelor's degree in Marine Engineering.

Q. And, where did you secure your Master's degree? A. From the Stevens Institute of Technology in Hoboken, New Jersey.

Q. And, where did you secure your Bachelor of Science degree? A. From the United States Merchant Marine Academy in Kings Point, New York.

Q. Now, would you tell the jury, Mr. Pomerantz, how you got interested in this Westinghouse Doctoral Program? A. While I was at the Stevens Institute of Technology, near the end of my senior year, I was aware of several representatives of several industrial firms coming onto the campus to interview prospective employees.

And, a friend of mine told me that the Westinghouse Electric Corporation in Pittsburgh had a program where

it was possible for an employee to go to school part time while he was working at the plant.

That is how I became aware of the program.

Q. Did you then seek employment with Westinghouse? A. Yes, I did. I saw the interviewers on the campus, and they arranged for me to go out to the Westinghouse Bettis plant for a one-day visit.

[36] Q. And, what occurred on this one-day visit?

A. While I was at the Westinghouse Bettis plant, I was interviewed by several members working at Westinghouse, where they would ask me questions about what type of engineering I was interested in. And, I would ask them questions about what type of work was being done at Bettis. I gave them my academic records.

A few people asked my why I wanted to continue my education. I told they why I thought it was important in this day for engineers to keep abreast of modern technology. And, that concluded the day.

Q. What was your academic record at Stevens Institute? A. I believe I received about ten A's and two B's, and I was an honor student at the United States Merchant Marine Academy.

Q. Were you then offered employment at Westinghouse? A. Yes. I was offered employment at Westinghouse, and I accepted.

Q. In what capacity were you employed? A. I was hired in a category called associate engineering.

Q. And, what branch of Westinghouse? A. I worked in a section which was then designing a nuclear reactor to be installed at Shippingport, Pennsylvania. I

[37] was in what is called the heat transfer and fluid flow section.

Q. Is this part of Bettis? A. Yes. This was a section in the Bettis Atomic Power Laboratory.

Q. And, what was the nature of your work? What was the nature of your work if you are free to state it at this time, or was your work classified? A. Oh, no. I was in a project that was not classified.

This project—or the purpose of the project—was to design and have constructed a nuclear reactor to be installed in the Shippingport plant which is nearby here owned by the Duquesne Light Company for the generation

of electricity. And, my duties were to design certain portions of the nuclear reactor.

Q. Would you call that developmental research? A. I would call it developmental research, yes. It was research and a developmental type of activity.

Q. Mr. Pomerantz, you were, of course, aware of the Doctoral Program at Westinghouse at the time when you began your employment? A. Yes, I was.

Q. When did you enroll under the program? A. At the same time that I began employment at Bettis, I was told that I would have the program offered to me.

[38] And, I entered Westinghouse employment in July, and I started school at the University of Pittsburgh on the program in September of that year.

Q. Then, in order to start school at the University of Pittsburgh, what did you have to do? A. I had to go through the enrollment procedure outlined in the catalogue published by the University of Pittsburgh. I had to obtain my records from my previous schooling and send them to the University of Pittsburgh.

And then, these records had to be accepted by the people in the mechanical engineering department. That is where I studied at the University. And then, once that was accepted, I was accepted as a student.

Q. From September then, how long did your studies—as distinguished from research—continue at the University of Pittsburgh? A. I took formal courses at the University of Pittsburgh from September 1957 to, I would say, January 1960—no, that was 1961, rather.

And then, a few months later, which would be about October or November of 1961, I started on my thesis work. So, the course work took approximately four years.

Q. Now, in 1957 when you first began at the University of Pittsburgh, would you tell the jury what you did as between the University of Pittsburgh and your

[39] employment at Westinghouse, time-wise? A. Well, during that period of time, I would be going to school and taking two or three courses, and during a four-day work week I would be working at Westinghouse designing these parts of the nuclear reactor for Shippingport.

• • •

[40] Q. Were these courses that you selected to take at the University of Pittsburgh the regular curriculum at the University? A. Yes.

Q. And then, this continued—this course of study or classroom study—until what year? A. The formal course study ended in 1961.

Q. And, during this period, you were working four days a week, you said? A. Yes.

Q. Were you being paid by Westinghouse? A. Yes, I was.

Q. And, of course, you paid taxes on that salary? A. Yes, I did.

• • •

Q. Now, during this four-year period, did you have to meet certain scholastic requirements? A. Yes. There were scholastic requirements. In order to stay on the program, the student had to be above average.

I don't recall the exact average that he had to have, but it was higher than one would normally need.

[41] Q. This is a requirement imposed by whom? A. This requirement was imposed by Westinghouse.

Q. And, this was a requirement that your grades had to be of a certain stature? A. That is right.

Q. Either a B or an A or a B-plus or something like that? A. Yes.

• • •

Q. Mr. Pomerantz, I show you what has been marked Plaintiffs' Exhibit 1. Would you just tell the jury generally what that is? A. This is a list of general rules and regulations and the purpose of the Westinghouse Bettis Fellowsihp Program. It was printed in 1957 on December 18th.

It is a set of rules put out to inform the people on the program and other people what the program consisted of.

Q. I show you now Plaintiffs' Exhibit 2 and ask you to tell the Court and jury what that is? A. This is

[42] another set of rules about the Westinghouse Bettis Fellowship Program, published internally in Westinghouse.

It is dated July 21, 1960, which happens to be my birthday.

But, it is another set of rules. They had revised the old set and put in a new set of rules.

Mr. Larrimer: If the Court please, it has been stipulated that Plaintiffs' Exhibits 1 and 2 may be offered in evidence. And, I so offer them.

Mr. Arkin: No objection.

The Court: Let Exhibits 1 and 2 be admitted in evidence.

By Mr. Larrimer:

Q. Mr. Pomerantz, as a part of your participation in this program, were you also required by Westinghouse to agree to employment subsequent to your completion of your degree work? A. I signed an agreement which stated that after my leave period, I would come back into the employ of Westinghouse for a period of at least two years after I returned.

Q. And, did you so comply? A. Yes.

Q. Now, let's get into the program itself. You were employed as an associate engineer, I believe, in 1957?

[43] A. Yes.

Q. Is that a title which carried with it a certain rate of compensation at Westinghouse? A. That is correct. For each title or type of engineer, they have a range of salary, and it is set up so that a person's salary would then be between a lower and an upper limit in that range. Each title defines a range of salary.

Q. Were there other associate engineers at Westinghouse receiving the same salary as you? A. Yes.

Q. And did all of these associate engineers participate in this program? A. No.

Q. So that, you received the same compensation as the other associate engineers? A. As far as I know, I did.

Q. Now, when you went on the leave program, in order to go on this program what requirements did you have to meet insofar as the University was concerned? A. Well, as far as the University was concerned, I had to have passed my qualifying examinations, which I did.

Q. Which was what? A. These are examinations in my skills and in engineering. I was tested in five

[44] categories of engineering. And, I had to receive a passing grade in all five categories.

Q. What were those five categories? A. They were heat transfer, fluid flow, thermodynamics, stress analysis, and vibrations.

I also had to satisfy the language requirements, which meant I had to be proficient in a foreign language. And, I passed the examination for that.

Also, I had to have a thesis topic which was acceptable to the faculty. And, previous to going on leave, I took a course which was designed to search out a thesis topic.

And, the procedure for the student—which I was at that time—is to look through the literature of the specialty of engineering in which I was interested, and to try to find where there were some problems that might be interesting.

And, I would work very closely with a member of the faculty at the University of Pittsburgh, and he would guide me, and we would come up with a topic that he felt was acceptable and I felt I would be interested in working on.

And, as soon as these met his approval, he had agreed to be my thesis advisor. This was the final requirement.

Q. Who was your thesis advisor at Pitt? A. My thesis advisor for the major portion of the thesis was
[45] Professor Yates.

Q. Do you recall, Mr. Pomerantz, what salary you were receiving immediately prior to the time you went on your leave of absence? A. Yes. Before I went on my leave of absence, I was receiving $800 a month salary.

Q. And, what was the amount of the allowance granted to you during your leave of absence, if you recall? A. It was $630 a month.

Q. Was this the amount specified under this Exhibit 2 that you referred to? A. May I just take a look at that? I am not sure whether that was the specific document.

Q. I show you the last paragraph. A. Yes, this is it. It was based on whether I was married and how many children I had.

Q. In other words, the $630 was determined in what manner under this outline? A. It was determined by my family status rather than anything that I had done before or what I was working on.

Q. Was $630 the maximum amount? A. Yes.

Q. Now, you testified that you discussed a thesis topic with your faculty advisor? A. Yes.

[46] Q. What was the topic that you ultimately decided to explore? A. The name of the topic was the effect of increased gravity on film boiling.

This is a heat transfer problem. The area of film boiling—and actually you may be familiar with it— is similar to dropping some water on a hot frying pan. Usually a cook tests whether the frying pan is hot enough in this manner.

If the bubble dances around on the frying pan, that type of boiling is called film boiling. And, this was the topic that I picked in conjunction with my thesis advisor.

Q. Would you tell the jury how you came about to select this particular topic? A. Well, I selected this topic after looking into the literature in heat transfer and fluid flow. I was interested in heat transfer and fluid flow, and I had some friends who had done some research at the University of Pittsburgh.

And, after looking at the literature, I saw that there was no information about the effect of increased gravity. And, by increased gravity, this would be something, for example, if someone was in an automobile and it was accelerated rapidly, that you would be pushed back into your seat. Well, that is due to acceleration or increased gravity.

[47]

Q. Mr. Pomerantz, did Westinghouse tell you to study this particular topic? A. No. I had no contact whatsoever with my supervisory people at Westinghouse while I was picking the topic.

Q. Who claimed ownership of the selection of this topic? A. Well, I claim it.

Q. You claim it. Was there any effort at all on the part of Westinghouse to compel you to select a particular topic? A. No, there was none whatsoever. No one came to me or told me or implied that I should pick a topic that they would be interested in. I was entirely on my own.

Q. When you selected this topic, did you then submit it to your faculty advisor or was he aware of it, or was the selection process a joint process? A. It was a joint process. Actually, I had to make up a report describing what I wanted to study and why, and he helped me with the report. And then, he approved the final report.

[48] Q. This was a written report? A. A written report to my faculty advisor, yes.

Q. And, what did this report report on? A. It stated where I thought there was a need for more knowledge, or

extension of knowledge, how I proposed to go about getting the information, how I proposed to solve the problem, and in essence why I wanted to study this particular topic.

Q. Did the report also contain a suggested requirement as far as equipment is concerned? A. Well, the report did contain requirements for instrumentation and certain pieces of equipment. I needed some test equipment for my thesis.

Q. To your knowledge, did this thesis topic solve any problem that was then confronting Westinghouse at their Bettis plant? A. None whatsoever to my knowledge. In fact, it was a type of boiling which at that time Westinghouse at Bettis would want to stay away from, because it meant they would have been in trouble if they had this happening in one of their reactors.

Q. Now, was there any notification given to Westinghouse of this particular topic that you chose? A. Well, yes. Before going on leave, I had to inform the people administering the program what I was going
[49] to be studying during my time off. And, I informed them, and probably in a written communication.

• • •

[50] Q. Where did this take place? A. This took place in a building about a mile from the University of Pittsburgh campus. It was owned by the University of Pittsburgh.

• • •

[51]

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Q. How long did you conduct this type of research—for what period of time—when you started your leave? A. For nine to ten months. It took me maybe a month or two to build the experimental apparatus with the equipment I was given, and it took me a long period of time to get the information that I wanted.

The total leave period was about nine or ten months.

Q. And then, you had to submit a written report, is that right? A. Yes.

Q. Were you writing this report at this time? A. I had started writing it. I had an outline before I started so I would know what information I needed. And then, I

started seriously writing the report in about my eighth month of the leave.

I continued writing it throughout that time and then went back to Westinghouse. And then, at night I would go home and work on the thesis.

And, I kept writing on it until about, I guess
[52] it was November of that year. That would be about two months after I had been back at Westinghouse before I had finally put it together and submitted it for approval to the University of Pittsburgh.

Q. Now, to whom would you submit this report? This is called a thesis report? A. Yes. A thesis or dissertation. And, I submitted it to my advisor. He had formed a committee of about himself and four other professors, and they each read the dissertation or thesis, and they sent me back any of their compliments or suggestions.

• • •

[53]

• • •

Q. During this nine-month period, what was your contact if any with Westinghouse? A. Well, there was no official contact with the company or the plant. Some friends of mine who worked there I would see socially.

Q. Did you perform any duties for Westinghouse? A. No, none whatsoever.

Q. Did you have any regular employment duty during this nine-month period? A. No, nothing, no obligation at all. I didn't have to show up at the plant until my leave was finished.

One thing I did have to do, and that was periodically to send in progress reports to the people at Westinghouse who administered the program. They wanted these progress reports to make sure that I was making progress, just as my thesis advisor wanted.

Q. And, what would a progress report consist of? A. Well, it might be a one-page report which would say that during the past three months I collected data or started an
outline, and during the next three months I expect
[54] to finish the first phase. That would be it, so that they would know that I was making technical progress.

Q. Now, you stated that this thesis topic, after you have successfully defended it, is then published and available for inspection? A. Yes. It is published in a sense that the University binds a copy and places it on their library shelves and indexes it so that anyone who wants to read it can read it.

In addition, I also chose to take my thesis and publish what is called a technical paper. I belong to a technical professional society, and I feel that the information that I obtained during this thesis would be of interest to engineers throughout the whole country.

So, I submitted it to them for publication. They accepted it and it was published in the national magazine that goes to engineers.

And, I also presented it at a technical meeting where engineers from all companies and all industries would be present. So that, everyone has access to the information now.

Q. Would this information be of any more value to Westinghouse than it would be to General Electric or some other company? A. No, it wouldn't be of any special value to Westinghouse. It is available to anyone. There is no special value that it has to Westinghouse.

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Cross-Examination

By Mr. Arkin:

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Q. We were discussing the area in which you worked in Bettis prior to your educational leave. A. Yes.

Q. Would you describe that? A. The work that I did was to design a nuclear fuel element specifically. This was the most important category.

Q. Now, how does that relate to this heat transfer and fluid flow? A. You mean why was it in this section?

Q. I would like to know what the area is about. A. Well, the nuclear fuel produces heat and the nuclear reactor has water going through it to carry the heat away. And,

in order to calculate how hot the fuel element is,
[57] one has to know how to determine the temperature of the fuel element. That is the heat transfer portion.

And, the fluid flow is to determine how the water goes by.

Q. Well now, what kind of work does Bettis do—that is the Bettis Laboratory—in general? A. They design nuclear reactors for the Atomic Energy Commission.

Q. Now, your thesis topic, was that not also in the heat transfer field? A. In a broad general sense, yes.

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Q. Now, were you not urged to consult with the supervisors of the Bettis project regarding your choice of a thesis topic? A. No one asked me to do that.

Q. Is there not a statement in the statement of purpose and general regulations which suggests that participants discuss with their Bettis supervisors the topics that they intend to study? A. (Pause)

Q. On page 4, paragraph 3, if you are on the same one I am on—

The Court: What are you on? Nobody else knows.

Mr. Arkin: It is Plaintiffs' Exhibit 2, page 4, paragraph 3.

The Witness: It says, "Each participant is urged to explore fully the possibility of conducting his doctoral dissertation in an area of technical interest to Bettis".

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Q. On page 5, there is a statement regarding educational leave and the AEC relationship. Were you aware that your educational leave had to be approved by the Atomic Energy Commission? A. Yes.

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Q. Were you also covered by the employees' pension plan while you were on educational leave? A. I don't recall.

[61] Q. Were you covered by any employees' plan for medical insurance, like Blue Cross? A. Yes, I think so.

Q. Do you know whether or not you were eligible for stock options pursuant to the Westinghouse plans? A. I don't know.

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Q. I realize that. What I am asking is whether or not Westinghouse restricted your choice of univer-

[62] sities for the entire program? A. I think so, yes. I think I could only go to the University of Pittsburgh for mechanical engineering.

If I had wanted to choose another subject, I could have gone to Carnegie Tech.

Q. Could you have chosen a subject such as philosophy or psychology? A. No. The subjects were limited to what was contained in a paper that someone read earlier in this courtroom. I don't recall whether it was in the opening argument, or what.

But, there were certain restrictions to engineering. Of course, engineering is a very broad field, containing mathematics, physics, metallurgy and a few other things, and which they are also broad fields which one can study. There are many things in engineering.

Q. Are these all fields from which the Bettis Atomic Power Laboratory draws its personnel, or from which its personnel are drawn? A. Yes. Well, the subjects I have outlined cover almost everything in technology.

Q. You mentioned that you signed an employment agreement? A. That is correct.

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Q. I hand you Defendant's Exhibit 1 and ask you to look it over and look at your signature.

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Q. Is it your signature? A. It looks like it. I would say yes, that it is my signature.

Q. Is that an accurate, true and correct copy of the original employment agreement that you signed? A. To the best of my knowledge, it is.

Mr. Arkin: Your Honor, we move Exhibit No. 1 into evidence.

Mr. Larrimer: No objection.

The Court: Let it be admitted.

By Mr. Arkin:

Q. Now, that agreement provided that you would work for Westinghouse for two full calendar years after you completed your educational leave, is that not so? A. Two calendar years from the date I assumed the duties that they assigned me, yes.

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Q. Now, when you went to Bettis for that interview, were you being interviewed for a job only or for the program also?

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Q. Was your purpose in going to Bettis to be interviewed for both? A. Yes.

Q. Is it fair to say that you were interested not only in a job but also in a job which would allow you to continue your education? A. Yes.

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Q. When you began your leave period, were you written a letter explaining the requirements of the leave period and explaining these reports that you were supposd to forward to Westinghouse? A. I don't remember. I probably did get some notice. Otherwise, I wouldn't have filed the reports and the things like that.

But, I don't exactly recall getting something. There is something spelled out in these regulations.

Q. May I hand you a letter to refresh your memory, perhaps? A. Yes. This looks like a letter that was sent to me and which I received, because it outlines what the progress reports should be.

Q. Did you keep the original of this letter?

[68] A. I don't know. I probably threw it away after I finished the course.

(The document was marked as Defendant's Exhibit 2 for identification.)

By Mr. Arkin:

Q. Now, referring to this letter, to refresh your memory, what were the requirements of the reports that were required? A. It says, "The format of your bi-monthly progress report should be as follows: Major accomplishments since the last report". I am just going to have to abstract these. I will leave out what I don't think is important.

"Deficiencies affecting your progress that are beyond your immediate control; identification and statement of your problems within the scope of your control and the recommended or planned solutions, together with a brief analysis of why the solution was selected;

"Laboratory or University actions that adversely affect your operations; general suggestions for improvement which are not within your area of control."

That covers what was supposed to be in the bi-monthly report.

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Q. Now, you began your leave in 1961, didn't you? A. That is correct.

Q. When you filed your tax return for 1961 in
[71] 1962, how did you report these payments? A. I reported them. They were included in my W-2 form.

Q. Did you report them as wages or salary? A. Yes.

Mr. Arkin: No further questions, Your Honor.

Redirect Examination

By Mr. Larrimer:

Q. And, you then filed a claim for refund? A. Yes, I did.

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Q. Now, Mr. Pomerantz, it has been brought out that you signed an employment agreement by which you would return to Westinghouse at the end of your educational leave? A. Yes.

Q. Now, did you in fact return to Westinghouse? A. Yes, I did.

Q. Did you go to the same job that you had before the leave? A. No. I went to a completely different aspect of engineering.

Q. You did not go back to the same job? A. No, I did not go back to the same job. I was in a different project and doing a different type of work.

Q. Then, how did you get to this new job? By what process? A. Well, it was almost as if I was a new employee coming in for a job. I asked for a certain type of assignment, and they said that they had openings and they would see if they could give it to me.

And then, a few weeks later, they told me I
[73] could have this position.

Q. And, what was the rate of compensation for this new job? A. I believe it was slightly higher than what I had. It was $830 a month, I think, as the pay.

Q. What was your title? A. My title was engineer.

Q. Engineer? A. Yes. That is higher than associate engineer.

Q. And, you were compensated for the work that you did for Westinghouse under this employment agreement? A. Yes. When I returned, I was getting a pay that was approximately what other people who had not been on the were getting for the same type of work with the same type of experience.

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RICHARD E. JOHNSON

called as a witness in behalf of the Plaintiffs and being duly sworn, testified as follows:

Direct Examination

By Mr. Larrimer:

Q. Would you state your name? A. Richard E. Johnson, Sr.

Q. Where do you live, Mr. Johnson? A. My full address is 6729 Still Meadow Lane, Cincinnati, Ohio.

Q. And, how long have you lived there? A. Since the first of October. That is a month and a half.

Q. Do you have a family? A. Yes, I do, a wife and six children.

Q. How old are you, Mr. Johnson? A. Thirty-eight.

[76] Q. And, are you employed presently? A. Yes, I am.

Q. By whom? A. The General Electric Company, Flight Propulsion Division, Cincinnati, Ohio.

Q. And, whene did this employment begin? A. June 13th of this year.

Q. 1966? A. 1966, yes.

Q. What was your prior employment? A. I was employed as a senior engineer at the Westinghouse Atomic Power Laboratory, West Mifflin, Pennsylvania.

Q. And, you are one of the Plaintiffs in this case? A. I am, sir.

Q. Now Mr. Johnson, when did your employment with Westinghouse begin? A. In June of 1956.

Q. And, what was your education prior to this time? A. In June of 1956 I received a Bachelor of Science degree in Metallurgical Engineering from Carnegie Institute of Technology.

Q. This was the first degree that you received in engineering? A. Yes, sir, or in anything else.

[77] Q. What was your prior employment? A. It was with United States Steel Corporation in the Homestead District Works.

Q. In what capacity? A. In various capacities throughout the inspection and metallurgical departments in the plant.

Q. Is this where you developed an interest in metallurgy? A. A real and abiding interest, yes.

Q. And, tell us how you became aware of the Doctoral Program with Westinghouse? A. In the spring semester of my senior year at Carnegie Tech, I was asked into the office of Professor Robert Mehl. who was the head of the metallurgical engineering department and also at the same time was the dean of graduate studies at the school.

He asked me if I was going to make application to graduate school. And, said I would love to but I couldn't support my family.

And, after quite some lenthy discussion, he advised me that, although not yet made public, there was to be forthcoming a Fellowship Program with the Westinghouse Atomic Power Laboratory, and suggested that although it might take me more time to get my degree, I might be able to support the family and should look into it.

I said I would be glad to. And then, I believe
[78] he took the initiative and some arrangements were made for me to be interviewed for the program.

Q. Were you then interviewed? A. Yes, sir, I was, in the spring of that year.

Q. And, where did the interview take place? A. At the Westinghouse Bettis plant.

Q. At that time, what was your purpose in seeking the interview or going to the interview? A. It was twofold, to seek employment as an engineer and to seek a position on the Fellowship Program.

Q. Now, in order to get into this program—this Doctoral Program at Westinghouse—was there a scholastic standard you had to meet? A. Yes, sir. I had to be accepted by the graduate school at Carnegie Tech.

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[79] Q. Were you accepted in this program?
[80] A. Yes, I was.

Q. At Westinghouse? A. Yes.

Q. And, when did your enrollment at Carnegie Tech begin? A. In September of 1956.

Q. 1956. And, when did your employment at Westinghouse begin? A. In June of 1956.

Q. June of 1956. Now, you have heard Mr. Pomerantz testify. Did your course of study take any length of time? And, your classroom study I am talking about. A. Yes. I engaged in a program which involved four years of essentially half-time study, which then equipped me to take the qualifying exam of which I spoke.

Q. During this four-year period, Mr. Johnson, what were the subjects or what were the general nature of the subjects that you studied? A. I studied courses which were basically what the department calls physical metallurgy as opposed to process or extracting metallurgy, but with certain extracting metallurgy minors.

I also had courses in mathematics, physics and chemistry. I probably could name them, but I am not sure that that is pertinent.

[81] Q. Were these classroom studies? A. They were, sir.

Q. Did you have textbooks? A. We did, sir.

Q. Were there other students? A. Yes, sir.

Q. Some of whom were not Westinghouse employees? A. Most of whom were not Westinghouse employees.

Q. Were these students regularly enrolled at Carnegie Tech? A. Yes, sir. They were in more than one category. Some were regularly enrolled for individual courses, some as evening school students, and others who were full-time degree candidates.

Q. Now, Mr. Johnson, were you a candidate for a degree? A. Yes, I was.

Q. And, did you pursue this classroom study to secure that degree? A. Yes, sir.

Q. Who determined, Mr. Johnson, what studies you should pursue? A. I did. However, I might add that because I did have this advantage of having been an undergraduate at the school. I was able to select my

[82] thesis advisor my first year in graduate school and we actually worked out a plan or strategy which covered the four years of classroom work and on into the thesis year.

We worked that out during the first year and, I believe, during my first semester while actually in graduate school.

Q. In other words then, these classroom studies were of regular subjects and of the regular curriculum of Carnegie Tech? A. That is correct.

Q. Were all students graduate students in these classes, if you know? A. There may have been some exceptions. They were courses offered to graduate students; let's put it that way.

Exceptional students may have been permitted in them. I wouldn't know.

Q. Did you receive a grade? A. In each course, yes.

Q. You took tests? A. I took examinations in each course, yes.

Q. Was there anything different in your attendance at these classes than the attendance of the other students? A. Not at all.

Q. Now, how long did this take, these classroom
[83] studies? A. Four years—four school years.

Q. From 1956 until 1960? A. Until the spring of 1960.

Q. Now, during this period, I believe you stated that you were able to select a thesis topic? A. I did.

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Q. What was the thesis topic that you selected? A. The thesis topic I selected, which I worked on during the educational leave, was the effect of hydrogen on the internal fraction of pure Zirconium.

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Q. But, how did you come about to select this topic? A. Through my background and experience as a practicing engineer.

Q. Is this a metallurgical exploration? A. Yes, it is. It was intended to be experimental in nature.

Q. Now, Mr. Johnson, did anybody at Westinghouse tell you to explore this particular subject? A. No, sir.

Q. Was there to your knowledge the same exploration being conducted at Westinghouse? A. No, sir.

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Q. And, your educational leave of absence began in 1960, I believe? A. Right.

Q. And continued into 1961? A. That is correct.

Q. During this period, Mr. Johnson, were you doing research on this Zirconium topic? A. That is right.

Q. Did you pursue this to conclusion? A. No, sir.

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[93]

Tuesday Morning,
November 22, 1966,
Jury Present.

* * *

(Richard E. Johnson was recalled as a witness and testified as follows.)

Direct Examination (Continued)

By Mr. Larrimer:

Q. Mr. Johnson, I believe your testimony terminated yesterday on the subject of your thesis topic which related to Zirconium.

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Q. Is this in the field of metallurgy? A. Yes, sir.

Q. Mr. Johnson, would you tell the Court and jury how you came about to select this particular subject? A. Yes, I will be glad to. The subject actually evolved over some years, even prior to the time at which I became a metallurgical engineer.

While working in the steel mill, I observed, first hand, the catastrophic effects of having gases such as hydrogen dissolved in metals. The metals can actually fracture under trivial loads.

And, I became aware of second hand information about how the wonder metal Zirconium can be affected by absorption of gases such as hydrogen, nitrogen, or oxygen.

One can take large sheets of metal and, under certain conditions, one can break them as easily as a glass cutter breaks glass in making a window pane for us.

So, I was very interested in gases dissolving in metals before I even received the Bachelor's degree in Metallurgy.

Q. Was this before your employment with Westinghouse?

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A. Well, I worked there for five years immediately preceding my employment in Westinghouse and while I was going to school full time. So, it would be during that tenure, I would say, without putting a specific date on it.

Q. Well, did this interest then continue over? A. Yes. While I was with Westinghouse, I retained the interest in

gases and metals, but then became somewhat of a specialist in engineering, or what I am called—and called by others—a mechanical metallurgist.

My thesis topic then was in the field of mechanical metallurgy, the mechanics of materials, and it specifically had to do with the mechanical behavior in what we call internal friction.

That can be illustrated by a simple experimental technique involving a wire and a bar with weights on it. Vibrations of the wire measure the changes in mechanical properties and gases absorbed by the metal under vacuum.

Now, first of all, I planned to do a thesis on the effect of hydrogen in titanium, but it turned out, after I was with Westinghouse for I think about a year and a half, a paper
[96] was published in the German Metallurgical Society magazine by the name of Zeitschrif fur Metallkunde which essentially did what I had in mind. It described the effect of internal friction on titanium by virtue of absorption of hydrogen.

So, I changed my thesis topic to direct my attention to Zirconium, the sister metal of titanium. And, I picked up one aspect of hydrogen with this metal that the German authors had not picked up, and that is the rate of change of the hydrogen with the Zirconium into Zirconium hydroxide, which is a precipitate, such as rock candy is a precipitate from solution of sugar and water.

So, I decided to pursue this subject, switching from titanium to Zirconium, and studying those aspects of the technique not covered by the German authors.

Q. So, you had originally considered a thesis topic originally in titanium? A. Originally in titanium, and I changed it, yes.

Q. And, the reason you discontinued this consderation of titanium was— A. It was because the essentials of the work that I was going to do with titanium were published prior to my even going on educational leave.

Q. By a German author? A. Yes, three German authors.

Q. Was this a university publication? Do you
[97] know? A. No. This was work done in an industrial laboratory in Germany.

Q. Now, who was your faculty advisor at Carnegie Tech? A. Throughout this tenure, I had selected Dr. Horne. That is Dr. G. T. Horne.

Q. And, had you discussed with Dr. Horne your titanium idea? A. Yes, I had, sir.

Q. And, had you reached any tentative agreement or any kind of an agreement at all with Dr. Horne as to the feasibility of titanium as a thesis topic? A. Yes. We decided it was feasible. And, the feasibility was borne out by somebody else doing it first.

Q. Did Dr. Horne then conclude that this should not be pursued, about titanium? A. Well, he concluded correctly—and I concurred—that we couldn't do as a thesis something that had already been published.

However, as I say, we did see one aspect of the experiment which had not been in the previous publication.

And so, by changing to a different metal and somewhat changing the experimental concepts, we felt that there was a thesis here. And, that is what I pursued while on leave.

[98] Q. In Zirconium? A. In Zirconium, yes.

Q. How long did you pursue the thesis topic then in Zirconium? A. Well, throughout, let's say, the two years prior to going on leave, the one year while on leave, and about two years after returning to Westinghouse, roughly. And then, I gave it up.

Q. You did not reach an answer? A. I did not, no, sir.

Q. Is there a reason, Mr. Johnson, why you decided to give up this particular thesis topic? A. Well, yes, there is. The strategy that I worked out with the concurrence of Dr. Horne involved quite a lengthy experimental procedure.

Zirconium, I might add, when hot reacts with the gases in the air, and its properties are degraded. So, it has to be protected when heated from the atmosphere, and this involved some complicated experimental setups.

Now, we felt that the plan was feasible because prior to going on leave I was on a fellowship plan which was conceived with a minimum of one year—one calendar year—plus an additional year if necessary.

That is, I was anticipating up to 24 months of educational leave.

[99] Q. From Westinghouse? A. From Westinghouse. But, within a month prior to my original request to go on leave, the fellowship plans were changed and the possibility of going on leave for 24 months was cut down to 9 months maximum.

This left me with a very complicated experimental setup which required my full attention on at least an eight-hour day and sometimes a twelve-hour day at school.

I pursued this for nine months. And then, after returning to work, I was just going to school evenings, and weekends, and it was a losing battle. And I gave it up.

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Q. Did you have any connection at all with the Westinghouse Bettis plant physically during this nine-month period? A. Not physically, no, sir.

Q. How did you receive your stipends? A. In the mail, by check.

Q. Did you render any services to Westinghouse during this nine-month period on your regular job? A. No services whatsoeyer as an engineer, no, sir.

Q. Now, at the end of the nine-month period, then what occurred insofar as your activities were concerned? A. My activities at the school then continued only evenings and weekends.

I returned some very few days before the actual termination date of the leave. I was invited to come into the plant and be interviewed by managers and, I think, three or four operational units.

And, I was essentially interviewed as though I was a candidate for a position coming in from the outside. I selected a position mutually agreeable to me and
[102] to one of the managers, and was essentially rehired back into the plant as a practicing engineer.

Q. What type of work, or what project work, did you begin then immediately upon your return? A. I became active in the area of the mechanical properties of plant metals as opposed to the metals which go into the nuclear core.

By this I mean I was working on the nuclear pressure vessel and the piping and the apparatus which are incident to the operation of the nuclear plant.

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Q. And, what was the thesis topic that you pursued to success? A. The title was the influence of the system of geometry on fracture toughness.

Q. I am sure I don't know what that means.

[104] But, would you tell the jury and the Court how you came about to select this topic? A. Yes. Again, this is in the area of mechanics of materials. In this case, however, it has to do with what it takes to make a metal break, and to break in a brittle fashion.

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Q. Would you tell then the Court and jury how you came about to select the second thesis topic? A. Yes, sir. Again, as I say, this is in the area of mechanical metallurgy. And, this is just another one of the aspects of the mechanics of materials in which I am interested, such as fracture and fracture prevention.

And, I saw a need for this particular experiment based upon my experience as a practicing mechanical metallurical engineer. I discussed this with Dr. Horne and got his concurrence that this would, when completed, be acceptable to the faculty. He and I both agreed that it was a thesis and experiment which could be completed.

I therefore, with his concurrence, went ahead and did the experiment. And, within one year's time, I had a draft of my thesis in his hands.

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Q. Now, was there any effort by Westinghouse to direct this particular thesis topic as a subject of investigation? This last one I am talking about, the successful one. A. In a word, no.

Q. This was the sole judgment of you and Dr. Horne? A. That is correct.

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Q. Mr. Johnson, do you recall what your salary was immediately before you went on leave? A. Not to
[110] the nearest penny, or even to the nearest dollar. But, it was something slightly below $700 a month before going on leave.

Q. And, do you recall what the salary was when you returned? A. It was to the penny what it was before I went on leave, with the possible exception of a cost of living raise which may have occurred while I was away. This detail escapes me. There was a routine cost of living raise.

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Q. Is your thesis—or the results of your thesis—available now? A. Yes, sir. There are actual copies of the thesis available at the library at Carnegie Institute of Technology, filed according to their card catalogue system.

And, I will go one step further. The Bettis Laboratory saw fit to publish my thesis as a Bettis document. That is, they assigned a Bettis alpha-numerical number to it, and issued it through the usual AEC channels as something in the public domain.

That followed, of course, the act of publishing
[112] it at the school.

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Cross-Examination

By Mr. Arkin:

Q. Mr. Johnson, you testified that you first became interested in employment with the Bettis Atomic Power Laboratory while you were a senior in college? A. Yes, sir.

Q. Doing undergraduate work? A. Yes, sir.

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Q. Was one of the factors you considered whether or not you would take the job at Bettis with their health plan benefits that they offered? A. I beg your pardon?

Q. Their health plan benefits. A. Health plan?

Q. Were you not interested in the fringe benefits that they offered? A. I suppose everyone is interested in fringe benefits, yes. I don't think that was a consideration in getting employment there.

That is something one sort of takes for granted these days, that there will be some kind of fringe benefits, even if it is only getting time off to appear in court.

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Q. Now, all of these things—salary, the benefits of the company, and the Doctoral Program—were things you took into consideration in determining whether or not you would take the job? A. There is an order of preference, but I will answer a qualified yes.

Q. What order of preference? A. The Doctoral Program was most important, the salary second important, and the fringe benefits less important.

Q. In order to qualify for the educational leave
[116] under this Doctoral Program, you testified you had to sign a contract with Westinghouse? A. I did not. Or I don't believe I did.

Q. Did you sign what is called an employment agreement? A. An employment agreement?

Q. With Westinghouse? A. This is a patent agreement you are talking about?

Q. No, sir. Let me rephrase the question. I don't think we are talking in the same vein. A. I am afraid we are not.

Q. In order to qualify for the educational leave phase of the program— A. Oh, yes. For that, yes.

Q. You did have to sign a contract? A. An employment agreement, yes, for the leave phase.

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Q. Now, your employment agreement required you to stay in the employ of Westhinghouse for a period of two years after you returned from educational leave? A. That was the stipulation, yes.

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Q. Mr. Johnson, I am handing you a Xerox copy marked Defendant's Exhibit No. 3. Would you describe that? A. This appears to be a copy of the employment agreement signed by me prior to my going on educational leave.

Q. Is that your signature? A. I believe it is, sir.

Mr. Arkin: Your Honor, we offer this into evidence.

Mr. Larrimer: No objection.

The Court: Let it be admitted. Defendant's Exhibit 3 is admitted.

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Q. And, when did you begin on the program?
[120] What date? A. Well, I would like to think that I actually began when I started working with Westinghouse, which was June of 1956.

However, I believe, as a technicality, you can only say I began it as of September of that year when I actually began class work at school.

Q. September of 1956? A. Yes.

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Q. What was the amount of the payment made to you during the period of your educational leave? A. My memory tells me it was $630 a month.

Q. Was that payment based upon two factors; a percentage of your base salary, plus what is called
[121] adders, which is a formula based on your dependency status? A. I believe that is correct, sir, yes.

Q. Now, while you were on educational leave, did you retain any of the employee benefit programs which were available to you? A. Some, yes, and some, no.

Q. Well, how about the health plan benefits or the hospitalization? A. I am going to have to beg off on this because this is a matter of record. I recall that there was an option on something. I believe it was a pension plan that I could exercise an option to carry it or drop it. And, if I dropped it, to pick it up at a later date.

I exercised the option while on leave to drop all those things which I felt I could and was allowed to drop. And then, I picked them up again after I returned to full time employment.

Q. So, this was your choice? A. It was an option that was offered, and I took it, yes.

Q. Westinghouse allowed you to keep these things, or you had the option to drop them? A. As far as I know, this is a correct statement of the facts.

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Q. Were you limited in your choice of universities? Could you have gone to Duquesne? A. No, sir, it was a program with Carnegie Tech, and so advertised.

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[124]

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Q. All right. Now, while on the program were you limited in any way as to what field of study you could undertake? A. Yes. I think I can help you out and phrase it correctly.

I was limited to those subjects which were directed toward obtaining a PhD in metallurgical engineering.

• • •

Q. Before you took educational leave, you were involved in your work at Bettis in studying nuclear core materials? A. Yes, sir.

Q. Now, when I interviewed you last January, you told me at that time you were studying nuclear non-core materials? A. Yes, sir.

Q. Isn't it true that those subjects—those two subjects—differ very little? A. It depends entirely on one's frame of reference. I am a mechanical metallurgist. I
[125] was applying the techniques and principles of metallurgy to both core before leave and non-core after leave materials.

So, I would agree with you providing it doesn't enter a degree of confusion.

Q. In your field of interest then, both these subjects involve the study of mechanical properties of metals? A. Yes, sir.

Q. The thesis which you completed also involves the mechanical properties of metals, doesn't it? A. Yes, sir.

Q. Now, you testified, sir, that you received those pay-

ments during your educational leave period by check? A. I believe that is correct.

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Q. Were taxes withheld from that check? A. I believe they were. Yes, I believe so.

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[127]

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Q. You had also a requirement that you submit bi-monthly reports? A. Yes, sir.

[128] Q. And, you also had to clear your thesis proposal through Westinghouse? A. Through the technical information office, yes, sir.

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[130]

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DR. GERALD T. HORNE,

called as a witness in behalf of the Plaintiffs and being duly sworn, testified as follows:

Direct Examination

By Mr. Larrimer:

Q. Will you state your name? A. Gerald Terrence Horne.

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Q. And, what is your present employment? A. I am presently employed as an assistant manager in the research engineering division, Glass Research Center, Pittsburgh Plate Glass.

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[131]

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Q. Were you, previous to your employment at Pittsburgh Plate Glass, associated in any manner with Carnegie Tech? A. Yes, I was.

Q. For what period of time? A. I was a member of the staff of the Metals Research Laboratory from about 1951 as an assistant professor, and then as associate professor

I was in the Department of Metallurgical Engineering from about 1952 to 1963—no, that was 1964.

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[132]

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Q. Now, Doctor, do you know one of the Plaintiffs in this case, Mr. Johnson? A. I know Mr. Johnson.

Q. And, in what capacity did you know him? A. I knew him as an undergraduate student and as a graduate student in the Department of Metallurgical Engineering at Carnegie Tech. And, more specifically, as a graduate student who did his thesis essentially under my direction.

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[133]

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Q. All right. What function would you have performed as a faculty advisor for Mr. Johnson? A. Well, "faculty advisor" is a term which covers everything from suggesting courses of study or essentially approving courses of study, to being a thesis advisor.

In this case, I was a thesis advisor and I was probably a faculty advisor worried about what courses he was going to take sometime previous to that, but I do not know when.

As his thesis advisor, which I think is the more specific question here, my duties were essentially to help Mr. Johnson to arrive at a thesis subject which would be doable and which he would not end up being unable to complete.

Also, to advise him during the doing of such a thesis, and to handle a certain amount of the logistics in getting that thesis approved.

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[135]

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Q. Now, were you aware of this Doctoral Program that was jointly sponsored by Westinghouse and Carnegie Tech? A. Yes. I know several of the students from Westinghouse who were a part of that in our department.

Q. Who in your department, if you know, established this program on behalf of Carnegie Tech? A. Dr. Robert F. Mehl was involved. He was head of the Department of

Metallurgical Engineering and he was involved as dean in the negotiations with Westinghouse as to what the program should be from Carnegie Tech's standpoint.

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[136] Q. Was there any change in the requirements of Carnegie Tech as a result of this program? A. None.

Q. Who determined the scholastic requirements that had to be satisfied before a PhD would be granted by Carnegie Tech? A. They were established before this program by Carnegie Tech and they were not changed.

Q. In other words, Westinghouse imposed no conditions or restrictions on the scholastic requirements of this PhD degree? A. No.

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[137]

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Q. Mr. Johnson has testified that he originally selected an investigation of Zirconium. A. Yes.

Q. Do you recall this? A. Yes.

Q. Would you relate how this came about, the selection of this particular topic? A. Well, I hate to make a speech, but to answer the question, if you will indulge me, in general a PhD degree guarantees to a prospective employer—somebody who is going to hire him—that this person is capable of doing "original research".

Now, in general, I teach—or taught at that time—courses to graduate students. And, they are courses of study describing what the world knew about a certain aspect, what had been found out, and what somebody else thought about a given subject.

Now, these courses are taken by graduate students and they are examined on them. And, these are tests
[138] of scholarship. It is not "Does the student know what other people have done" or "Does he understand what they have done", but it is an original approach. There is at the moment no other way that I know of to test original research other than to do it in this manner.

So, a PhD student comes down to doing his thesis, which is the original research accounting, and for which he is essentially responsible. It is normally a long, drawn out

process. He will spend somewhere between one year and three years doing it, and sometimes more than three years. He will get deathly tired of it, and he will be ready to throw it up. They all do sooner or later.

So, one of the things I look for in a student—or looked for—was an involvement by him in this problem, whatever the thesis problem was going to be. And, I would want to be assured it would be something he really wanted to know the answer to.

Now, the easiest way to get this is to let him dream up his own problem. If he thinks it up and if he gets involved in it, then he won't, a year and a half later, say "This is a lousy problem that some silly professor gave me and which I didn't want".

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Q. Was there any difference in the requirements which Mr. Johnson had to satisfy to get his PhD degree from Carnegie Tech as distinguished from the requirements for the other students? A. No, none whatsoever.

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Q. Dr. Horne, were you aware of other students who were in a capacity similar to Mr. Johnson, in that they were seeking the degree of Doctor of Philosophy in engineering from Carnegie Tech who were being subsidized while they were seeking this degree? A. Yes.

Q. Were the scholastic requirements any different for those students than for Mr. Johnson? A. No, they were not.

Q. Were the studies that had to be successfully pursued by those students any different than for Mr. Johnson? A. They were not.

Q. Were there any more or less conditions or restrictions, if any, imposed by the other grantors of the subsidies than by Westinghouse? A. Imposed on whom?

Q. On Carnegie Tech? A. Oh, no.

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[148] Cross-Examination

By Mr. Askin:

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Q. What these negotiations were concerned with was more or less the mechanics of the program? A. Agreed. The mechanics and almost certainly the money. And, almost certainly as well the—

[150] Well, Dr. Mehl spent a healthy hunk of his time making sure that these were ordinary graduate students, and that Westinghouse did not prescribe for them.

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[154]

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Q. Do you know if Westinghouse had any control over the specific thesis topics chosen by any of the three Plaintiffs? A. I can speak only for one directly. Over Mr. Johnson, there was none.

Q. Do you know whether or not there was a shortage of trained PhD personnel in metallurgical engineering in the 1960's? A. There was.

Q. A great shortage? A. The newspapers and the magazines indicated a tremendous shortage.

Q. Now, when we are speaking of persons with the records of Dr. Johnson, Dr. Pomerantz and Dr. Wolfe—people with B-plus or A records—was there a

[155] a great deal of demand for personnel with such records as theirs? A. As students, or as what?

Q. As PhD's? A. You mean having completed a PhD?

Q. Yes. A. There was.

Q. Now, who was interested in employing PhD personnel, by category? Was industry interested? A. Very much.

Q. And, education? A. Yes.

Q. There was an overall shortage at this time? A. Yes. We had recruiters attempting to recruit them from industry, government and other educational institutions.

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[157]

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RICHARD A. WOLFE,

called as a witness in behalf of the Plaintiffs and being duly sworn, testified as follows:

Direct Examination

By Mr. Larrimer:

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Q. Where are you presently employed? A. At Westinghouse Bettis Atomic Power Laboratory.

Q. When did your employment at Westinghouse begin?

A. In August of 1952.

[158] Q. In 1952? A. Yes.

* * *

Q. What is your educational background? A. I got a BS degree in metallurgical engineering from the University of Cincinnati in 1952.

Q. Did you then continue with your education? Did you get a Master's degree? A. Yes. I received a Master's degree from Carnegie Institute of Technology in 1956.

Q. 1956? A. Yes.

Q. At this time, were you employed by Westinghouse? A. Yes.

Q. Up until this time in 1956, had you secured any kind of a leave of absence from Westinghouse to continue your education? A. No.

Q. Now, do you now have a degree of Doctor of Philosophy? A. Yes.

Q. When did you secure this degree? A. In June of 1963.

Q. And, was this degree secured under this

[159] Westinghouse Doctoral Program? A. Yes.

Q. You are one of the Plaintiffs in this case? A. Yes.

Q. Mr. Wolfe, would you tell the jury how you became interested in this program? A. Well, when I obtained my MS degree, I made a decision that I would continue my education to obtain a PhD degree in the same department, the same field, metallurgical engineering.

So, I went to the head of the Department of Metallurgical Engineering, Dr. Mehl at that time, and inquired about it.

Q. Is this the Dr. Mehl that Dr. Horne has referred to? A. Yes. It is Dr. Robert F. Mehl, who was then head of the Department of Metallurgical Engineering and dean of graduate studies.

I inquired about the availability of a fellowship. And, during the course of the conversation, he told me of the Bettis Doctoral Program which then had not been made public, but whose arrangements were then being made.

Q. As a result of this information by Dr. Mehl, what did you do then? A. Well, in the course of that
[160] conversation, Dr. Mehl requested that I, rather than ask for another fellowship, apply since I was already employed at Westinghouse, and he suggested that I apply for one of the Bettis Doctoral fellowships or scholarships.

Q. Did you so apply? A. I did apply.

Q. What process occurred then? I take it you were accepted? A. I applied and I was accepted. And then, I enrolled the following fall. That would be the fall of 1956.

Q. At the time of your conversation with Dr. Mehl, had you then received your Master's degree from Carnegie Tech? A. Yes.

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Q. And, you began at what period of time? When did you begin the studies for your Doctor's degree? A. I began in the fall of 1956, in the fall semester.

Q. And then, how long would you have studied before your leave of absence? A. Well, because I had obtained a MS degree, I had already done a large part of the class work, or course work.

So that, I only had about two years, or about two and a half years, left of course work to complete.

Q. And, how did you complete this course work, timewise? A. Well, I completed it during a period of about two years, or two and a half years, on this relief time program, working part time and having eight hours a week off.

Q. You would work how many hours for Westinghouse? A. Thirty-two. And, there would be eight for school.

Q. You would have eight hours off? A. Yes.

Q. During this period of time, you were of course being compensated by Westinghouse? A. Yes.

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Q. Now, your leave period began, I believe, in 1960. What period of time did you have? A. One year, from March of 1960 to February 28, 1961.

Q. And, do you remember the amount of the stipend that was paid to you during this one-year period? A. Not really, no. It was somewhere on the order of $900, I believe.

Q. What was your thesis topic? A. Anomalous diffusion in body-centered cubic transition metals. That was the title of it.

The topic dealt with how fast atoms move around inside of solids, from one part of the solid to another, and how fast atoms diffuse.

Q. Did you reach a conclusion? Were you able to determine this? A. Well, the idea was to try to obtain data which would solve some problems and uncertainties and gaps in the knowledge that was present at that time.

Are you asking how successful was I?

Q. No. Let me backtrack there. How did you come about to select this particular topic as a thesis topic? A. Well, prior to going on leave, I talked to professors in the Department of Metallurgical Engineering.

[163] Q. At Carnegie? A. At Carnegie Tech, yes. I talked to them about thesis topics.

I went to those professors whose fields of endeavor were concerned with what I was interested in, and we discussed problems in physical metallurgy and what might be done to obtain data to understand more fully these problem areas.

After this discussion with several professors, I picked an area or a topic of problem that I was interested in, and then worked out a proposal for a type of research or a type of study which was agreeable to the thesis advisor I had selected.

Q. Had you been directed by any of the personnel at Westinghouse to select this particular topic? A. No.

Q. What control if any did Westinghouse have on the selection of your thesis topic? A. None on the selection.

Q. After a topic was selected, were you required to advise them of the topic? A. Yes.

Q. And, what was the purpose of this, if you know, of telling them what your topic was? A. I am not sure.

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Q. Did you in fact inform Westinghouse of your thesis topic? A. Yes. I submitted it for approval by the technical information office to show that it was publishable.

Q. And, would this have been done prior to your leave of absence? A. Yes.

Q. Was it approved? A. Yes.

Q. Were there any conditions or restrictions imposed on the approval? A. No.

Q. How were you advised of the approval, if you recall? A. I would guess in a letter.

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Q. Now, you heard the testimony of Dr. Horne. Did Dr. Paxton function in the same capacity with regard to you as Dr. Horne did with regard to Mr. Johnson? A. Yes.

Q. Did Dr. Paxton collaborate with you in the selection of this particular topic? A. Yes.

Q. Prior to the time that you went on leave—prior to the time that you took this twelve months leave of absence—what particular job did you have at Westinghouse? What were you working on at Westinghouse, if it is not classified? A. I was working in a department or a group, whose function was to find new and improved ways to fabricate or make fuel elements where the fuel element is that part of a reactor that contains the uranium.

Q. And, after you came back to work to Westinghouse, did you go back to work in the same group? A. No. I went into a different area. I went to work in ceramics rather than in metals.

Q. Now, Mr. Johnson and Mr. Pomerantz have each testi-

fied that they signed an employment agreement. Did you sign any such agreement? A. No.

[166] Q. Were you advised that you were expected to return to Westinghouse at the termination of the leave? A. I believe, yes, they expected me to return. And, I expected to return.

Q. When you returned, were you compensated at the regular rate upon your return? A. Yes, for my job classification.

Q. What was your classification upon your return? A. Senior engineer.

Q. Does that carry with it a designated salary? A. It carries with it a designated salary range.

Q. A range? A. For each job classification, there is a range in which a person's salary falls, yes.

Q. And, was your salary within this range? A. Yes.

Q. And, you received that upon your return and you have received your compensation since then for your designated title? A. Yes.

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Cross-Examination

By Mr. Arkin:

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Q. In order to refresh your recollection, I hand you Defendant's Exhibit No. 5. That is a copy of a letter that was sent to you, is it not? A. Yes.

Q. Do you recall receiving that letter? A. Well, not exactly. But, I am sure I did.

Q. Are you familiar with the contents generally? A. Yes.

Q. Like Doctors Johnson and Pomerantz, you also were required to make reports? And, I believe your reports were quarterly to Bettis while you were on educational leave? A. Yes. That was requested.

Q. And, on the last page of that letter, you said you didn't recall if you were informed that you were expected to return. Does that refresh your recollection? A. Yes. It states that.

Q. It states what? A. "Each participant is expected to return".

[169] Q. Did you honor that commitment? A. Yes. I am still there.

Q. Now, while you were on educational leave, did you lose any of your employee benefits? Did you lose your health insurance? A. No, I don't believe so. I don't recall exactly, but I don't think I did.

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Q. Did you lose any of your retirement benefits? A. No.

Q. Did you lose your life insurance benefits? A. No.

Q. What about your seniority? Do you know how that was handled? In other words, for nine months you were essentially out of the Bettis Laboratory, is that

[170] true? A. Yes. It was twelve months.

Q. Yes, twelve months. Did you then lose a year's seniority? A. No.

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[171]

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Q. Now, did you testify that the checks were mailed to you? A. No, I didn't testify to that.

Q. Were they? A. No, I don't believe so. They were mailed directly to the bank.

The Court: Mailed where?

The Witness: To the bank.

The Court: To the bank? You don't mean the bank got the money?

The Witness: Well, at Westinghouse—and I guess this true of many concerns—the employee has an option to have the pay sent to his house or to the bank where he has an account.

And so, mine were sent to the bank.

The Court: And, they were deposited in your account?

The Witness: They were deposited in my account, yes.

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By Mr. Arkin:

Q. All right. Now, the amount of those checks, was that based upon a percentage of your base salary plus

[172] adders for dependency status? A. It was based on marital status, number of children and base salary.

Q. Now, you began your educational leave before July of 1960? A. Yes.

Q. And, you have before you Plaintiffs' Exhibit 1, is that correct? A. No.

Q. No, excuse me. Here it is.

I hand you Plaintiffs' Exhibit 1, and ask you if those are the rules and regulations which governed your educational leave period? A. Since it is dated December 1957, I would say yes, I think it is, although they were changed from time to time. But, I believe this applied.

Q. Does that look familiar to you? A. Yes.

Q. This is a different program or a different statement of rules and regulations than that which applied to the other two Plaintiffs, isn't it? A. Yes.

Q. On page 5 of that exhibit you will see your reimbursement clause? A. Yes.

[173] Q. Now, does that not state that the stipend shall be equal to 70 per cent of your salary, plus adders? A. Yes.

Q. With a maximum additional allowance of ten per cent depending on your dependency and marital status? A. A maximum of 20 per cent.

Q. Yes, 20 per cent. So then, the maximum amount you could receive under this program was 90 per cent of your base salary? A. Yes.

Q. Is that what you received ? A. Yes.

Q. Now, the checks when they were deposited in your account, were they checks for the gross amount of 90 per cent of your base salary, or were taxes withheld from them? A. Taxes were withheld.

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Q. And, within the field of metallurgy itself, were you restricted as to your topic by Westinghouse? A. No, not at all.

Q. So that, a restriction in your thesis topic to metallurgy was a self-imposed restriction that you made yourself? A. Yes. I made that choice years before the program was developed.

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CAMPBELL C. YATES,

called as a witness in behalf of the Plaintiffs and being duly sworn, testified as follows:

Direct Examination

By Mr. Larrimer:

Q. Your name? A. Campbell C. Yates.

Q. You are professor at the University of Pittsburgh? A. That is correct. My title is Professor of Aero-Space Engineering in the Department of Mechnical Engineering.

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Q. Do you know Mr. Pomerantz, one of the Plaintiffs in this case? A. Yes, I do.

Q. How did you get to know Mr. Pomerantz? A. He was a graduate student in the Department of Mechanical Engineering at the University.

I was also his thesis advisor. By this I mean that I was the faculty member who was responsible to see that he did the proper type of work and that he followed through in his research for the degree of Doctor of Philosophy in mechanical engineering.

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[183]

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Q. Professor, would Mr. Pomerantz have had to have met any scholastic requirements in order to get in graduate school, to enroll as a graduate student? A. Yes. He would have had to have met our minimum requirements of a 3.0 average, as we refer to it, or a B average in terms of scholastic average.

If he did not have this—and I am not familiar with his background at this particular time in terms of his admission—we might have admitted him on probation. But, as I recall, I think that he probably met these requirements without any difficulty.

Q. And, are these requirements established by the University of Pittsburgh? A. They are established by the graduate faculty of the University of Pittsburgh, yes.

Q. Tell me, to your knowledge, Professor, did the Westinghouse Electric Corporation or the Atomic Energy Commission have anything to do with establishing these requirements? A. Not to my knowledge, they didn't, no.

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[185] Q. Now, how did you become aware of the thesis topic which Mr. Pomerantz had selected? A. Well, the matter of selecting a thesis topic is sometimes a rather devious trail.

Generally it happens this way. The student, first of all, has an interest in a particular specialization within the field of mechanical engineering. And—

Q. Excuse me. How did you become aware of this particular interest on the part of the student? A. From conversation with him and from contact with him as an advisor. And, his advisor previous to the time that I was his advisor had talked to him.

He would also indicate this field when he took his comprehensive examination. He would have indicated to us then that he was interested in a field of fluid mechanics or stress analysis or elasticity or one of the principal fields that we have in the department.

Q. All right. I was asking you about the selection of a thesis topic. A. Well, the faculty members also have an interest in certain specialized areas. And so, it becomes a problem of matching these interests.

The student, having an interest in a certain specialization, then discusses this interest with a faculty member.

And, there is, of course, a question of the
[186] suitability of a topic.

Sometimes the subject material will be suggested by the faculty member and sometimes by the student. In this case, I do not recall the specific details.

The department itself had considerable interest in the problem of boiling heat transfer. We were building a new facility at that time to do boiling heat transfer work.

And, this problem, whether suggested by Mr. Pomerantz or the faculty at the time, is along that line. It is a problem in boiling heat transfer.

Q. Was this a problem then of interest to the faculty at the University? A. Yes, very definitely.

Q. Would there not naturally then be a matching process between the topic selected and the faculty advisor? A. Yes. In general, it seems very obvious to me that we would not assign a faculty member to a student if the faculty member had no interest in the problem whatsoever.

Now, it may be that the problem is sort of on the fringe area of the faculty member's interest. But, nevertheless, there would be a one-to-one correspondence of interest in this topic to a certain degree.

Q. Now, after there had been a designation of a thesis topic, is it submitted to you as a faculty member
[187] as being his thesis topic? A. Well, what the candidate has to do is prepare a proposal, in effect, and this proposal is given to us in duplicate so that we can pass it out to a number of faculty members who form a preliminary committee to screen this topic and decide whether or not it meets the requirements of a dissertation.

Q. That is just the topic itself before there is any research ever conducted? A. This is prior to any research being conducted.

Now, the candidate, of course, to present this proposal must have made a thorough literature search to make sure that he is not proposing a topic which has already been done. That is, that he is not proposing to repeat work which is already in the literature.

The thesis requirement is that the man produce some new knowledge in the field. This must be original research. He must produce either a new method of solving

a problem, or a method of solving it better, or a manner of handling the problem in a more suitable, accurate or successful way.

It must be the actual product of new knowledge, so that he has done some research in the preparation of it. And, basically, we must be assured that there has been a strict literature search.

Q. Professor, who determines this as a necessity, [188] that it be new knowledge? A. The requirements of the University.

Q. The University of Pittsburgh? A. Yes. That would be in the requirements for the degree.

Q. And, what is the reason for this? A. Well, basically I will have to answer that, I guess, in answering what I believe the Doctor of Philosophy degree indicates.

That is, it indicates that this man has reached a level that he can handle the very complex problems, first of all. And, secondly, that he is capable of doing individual work and actually probing into the unknown. It indicates he has reached a degree of sophistication in his work that he can actually extend the frontiers of knowledge.

And, the purpose of the dissertation is for the man to prove this to the faculty of the School of Engineering.

Q. Is this then a testing apparatus or testing device? A. Partially, I guess. But, at the same time, it is basically a part of the educational process for this man, because it permits him now, without bounds of formal course work, to actually delve into a specialized area and increase his knowledge in depth in this particular specialization.

Also, it serves a twofold purpose. One, you [189] might say, is a screening purpose, to determine whether or not he is the caliber of man, intellectually and in terms of training and background, who should receive the Doctor of Philosophy degree.

But, secondly, it is a part of the learning process for him to learn how to adapt everything he has learned up to this time to the solving of a new problem.

Q. Now, who would make a decision as to whether a particular thesis topic would be acceptable to the University? A. That would be in the University of Pittsburgh, in our department. And, this varies somewhat from department to department.

There would be a committee which would screen this preliminary proposal and would decide whether or not this topic was saticfactory.

Q. Do you recall the thesis of Mr. Pomerantz? A. Yes. It was a problem dealing with film boiling, the boiling of liquids, and the involved acceleration.

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Q. You were advisor to other students who were candidates for the degree of Doctor of Philosophy? A. Yes.

Q. Did they similarly select a thesis topic? A. Yes.

Q. And, was the thesis topic similarly screened as to the necessary attributes as you have described? A. Yes.

Q. Was there any difference in the requirements which must have been met by Mr. Pomerantz with regard to his thesis topic than any other graduate student in

[191] your Department of Engineering? A. No.

Q. Professor, did you receive any communication at all from Westinghouse directing this particular thesis topic be pursued by Mr. Pomerantz? A. Not to my knowledge, no. I don't recall any such correspondence.

Q. Were any restrictions placed upon this to your knowledge, upon this thesis topic and the investigative process, by Westinghouse? A. You mean as the work was done at the University?

Q. Yes. A. Not to my knowledge, no.

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Q. Let's get back to the thesis itself. After the thesis topic was approved, was it successfully then concluded to your knowledge? A. Yes, it was.

Q. Do you recall how long this took Mr. Pomerantz? A. I believe it was in excess of nine months. I can't be any more specific than that. It was at least nine months.

Q. Very well. And, what was the procedure by which the investigative process was approved? A. You mean the results of the investigation and dissertation?

Q. No. How was it approved by the University? What was the procedure in defense of the thesis? A. Well,

after the man has completed his research,
[193] he must of course defend this as a part of his final oral examination. And, this defense is before a committee of the faculty.

Q. Excuse me. Let me interrupt. After he does his investigation, then he writes a report? A. That is correct. He must write a formal dissertation. He writes a thesis on this and presents it.

This volume has in it all of the background information and the literature search that shows that this problem is original. It also presents the purpose of his investigation, how he intends to do it, and then it presents the actual method in which he did the investigation, the results and the conclusions he formed from this investigation.

All of this appears in this bound copy eventually, or bound report.

Q. Then, what is the defense? A. Then, he must defend this before a committee. After it is written, the written version of it, of course, is available beforehand to the committee members. They are at liberty to read it.

And then, there may be questions on the part of any member. There could even be questions as to the suitability of the topic at that time if they cared to go back that far.

Q. Is any notice given to the public? Is the
[194] public invited to this defense? A. No, I don't believe so. I don't think there would be any objection to anyone who had a valid reason for wanting to sit in on one of these oral examinations.

Of course, in general the other members of the graduate faculty outside the school are invited. By that I mean that someone from the School of Education or the Department of Mathematics, if they wished to sit in on the examination, would be perfectly free to come in and observe the examination.

Q. And, Mr. Pomerantz successfully defended his dissertation? A. Yes, he did.

Q. And, was he awarded the degree of Doctor of Phiosophy? A. Yes.

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[197]

Cross-Examination

By Mr. Arkin:

Q. Professor Yates, you testified that the University controls the thesis in general? A. Yes. The University controls the thesis. And, by this we mean that we are the ones who approve the topic and say that this is appropriate as a subject for a dissertation.

Q. Do you know of any other control exercised upon the choice of thesis topics? A. Not at the University, no.

Q. Not at the University. You also testified that you had other students on subsidized study such as NASA grants? A. Yes.

[198]

Mr. Arkin: At the close of the Plaintiffs' evidence, the Defendant respectfully moves this Court to direct the jury to return a verdict for the Defendant upon the following grounds:

One, the Plaintiffs have failed to prove the primary purpose of the payment.

Secondly, the Plaintiffs have introduced no evidence as to the primary benefit derived from the studies.

Thirdly, the Plaintiffs have failed to prove that these payments were not compensation for past, present

[199] or future services, or for services under the direction and control of the grantor.

And, fourthly, the Plaintiffs have failed to prove by a preponderance of the evidence that the determination of the District Director of Internal Revenue was erroneous.

[203]

The Court: . . .

And now, we have a jury to decide it. So, we will let the jury decide it. . . .

The motion is denied.

[217]

CLYDE E. VOGELEY, JR.,

called as a witness in behalf of the Defendant and being duly sworn, testified as follows:

Direct Examination.

By Mr. Arkin:

Q. Dr. Vogeley, would you state your name and address for the record, please? A. Dr. Clyde Eicher Vogeley, Jr., 185 Peach Drive, Pittsburgh 36.

Q. By whom are you employed, sir? A. Westinghouse Electric Corporation.

Q. For how long have you been employed by Westinghouse? A. I have been employed by Westinghouse since 1944.

[218]

Q. What field did you work in in 1956? What office? A. In 1956, I was a senior engineer in the training group of the Bettis Atomic Power Laboratory.

Q. And, what is the training group? A. The training group is a group at the Bettis Atomic Power Laboratory that has cognizance for the training of Bettis personnel and customer personnel.

This includes giving course work in areas that are important to reactor engineering, and it also includes cognizance for the Doctoral and Fellowship Programs.

[219] Q. Are you familiar with the regulations of the Doctoral and Fellowship Programs? A. Yes.

Q. When did you first become familiar with those? A. Well, when I reported in 1956 to the Bettis Atomic Power Laboratory, one of the first tasks that I was assigned was that of putting the Doctoral Programs on a sound administrative basis. And, I generated the first set of rules and regulations.

Q. Do you mean that you wrote the first set? A. Yes.

Q. In order to write the first set, were you familiar with the purposes and ideals of the program? A. Yes, I believe that I can say that I was in the sense that I conferred

with my superiors to ascertain what those goals and those purposes were.

Q. Could you tell the jury what those goals and purposes were, sir? A. Well, I think they were twofold. One aspect of it was to attract to the Bettis Laboratory very bright young engineers and scientists. The other aspect was to upgrade people within the laboratory, people who were already there.

Q. Was that important to Bettis? A. Yes.

[220] Q. At that time? A. Yes.

Q. Why? A. Well, I think you can categorically say that in the world in which we live today—and even then, I think, and even more true ten years ago—that there was a shortage of this kind of people.

Q. What kind of shortage? Was it a serious shortage? A. I really couldn't judge that. I would say that the Bettis Atomic Power Laboratory felt that they needed more of this kind of people.

Q. What do you do now, sir? A. I am now manager of technical training.

Q. As manager, what are your duties? A. My duties are to manage the training group.

Q. Do you handle the day to day affairs of the training program, or is that handled by someone else? A. Well, the day to day affairs of the Doctoral and Fellowship Programs are handled by Mr. William Quinn, who reports to me.

Q. I see. Now, sir, do you know the source of the funds? A. The primary source of the funds is the Atomic Energy Commission.

[221] Q. Are you required in any way to report to the Atomic Energy Commission what you are doing? A. Yes. We do file reports with them.

Q. How often? A. Oh, it must be about—I can't answer that exactly. It depends on the nature of the report. I would say every six months.

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Q. Sir, do you know if the Bettis Atomic Power Laboratory has any contractual relationship with the Atomic Energy Commission? A. Yes. There is a contractual relationship.

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[222]

Q. Is it in writing? A. It is my understanding it is a written contract.

Q. Are you familiar with its terms? A. Not in detail, no.

Q. Are you familiar with its terms in regard to your particular area? A. Yes.

Q. Now, you testified earlier that you submitted reports to the Atomic Energy Commission regarding the program. What is the purpose of those reports? A. Well, they are status reports, really.

Q. Would you explain that, sir? A. Well, it is how many people are currently on the program, what has been the productivity of the program, and what has been the cost, and matters like this.

Q. Can you give me a general idea of how many persons you have had on this program since its inception? A. I think that the maximum number of people that were ever on the program was in the neighborhood of 112. In terms of productivity, I would say in very round numbers we have had 60 PhD's produced by this program.

Q. Now, sir, you testified that Mr. William Quinn runs the day to day affairs of the program?

[223] A. That is correct.

Cross-Examination

By Mr. Larrimer:

Q. Dr. Vogeley, you are a doctor in engineering? A. In mathematics.

Q. You stated the purpose of the program was two-fold; one was to attract people to Bettis, and the other was to upgrade those people already there.

Now, would it be accurate to say that the way you do this—the way you attract people to Bettis—is to offer them this Doctoral Program? A. That is certainly one of the attractions.

Q. Well, aren't we talking— A. It is to this kind of people.

Q. Well, aren't we talking about this Doctoral Program? A. If you are talking about this Doctoral Pro-

gram, it is one way of attracting bright young people to the laboratory.

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[225]

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Q. Would it be accurate to say that this is a program under which a person may attend a university or an educational institution as a student and secure a degree from that university while being subsidized by Westinghouse? A. Yes. He may attend the university as a student while receiving reimbursement from Westinghouse.

Q. Would you not agree with me, Doctor, that this stipend of $630 that is paid to these men while they are on their leave of absence is a living allowance to them while they are pursuing their research? A. It is a sum that is paid to them so that they can devote their attention to the completion of their dissertation.

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WILLIAM A. QUINN,

called as a witness in behalf of the Defendant and being duly sworn, testified as follows:

Direct Examination

By Mr. Arkin:

[226] Q. You are Mr. William A. Quinn? A. Yes.

Q. What is your address, Mr. Quinn? A. 709 Elina Drive, Monroeville, Pennsylvania.

Q. And, by whom are you employed? A. By the Westinghouse Electric Corporation.

Q. For how long have you been so employed? A. Since September 1957.

Q. What is your job with Westinghouse? What do you do? A. Well, I am staff assistant in the technical training department at Bettis.

Q. What are your duties? What does that entail? A. Administering certain training programs. And, included among these are the Bettis Fellowship and Doctoral Programs.

Q. You are the day to day administrator of these programs? A. That is correct.

Q. Do you select certain graduates to participate in the program? A. Well, the program works in this manner.

The graduates will apply through my office, at which time their qualifications are reviewed by a panel of senior technical members of the management at the Laboratory, who make recommendations as to whether these men
[227] are to be selected or not.

Q. Are you familiar with the criteria used in making such a determination? A. Yes, I am. I perform a preliminary review.

Q. What criteria are used to determine whether or not a person should be accepted into the program? A. We look for a person with a minimum undergraduate average of a B, and we look for a person with a graduate average, if he is taking graduate work, that out of four courses, he will have received three B's and one A.

Q. Do you know in what percentile of the class these people would be located in general? A. We seek to obtain people from the top ten per cent of the graduating classes.

Q. Do you require that the degree be held or sought in any particular field? A. The Bettis programs are only available in certain specific fields.

Q. Could you tell the jury what fields they are available in? A. Are you referring to the period back in 1960 and 1961?

Q. Yes, sir. A. At that time, the program was available only in the fields of mechanical, chemical, electrical
[228] and metallurgical engineering, and physics and mathematics.

Q. Now, as to the educational leave phase of this program, you have heard testimony that the purpose of that is to write a thesis. Is that correct? A. That is the purpose of the leave.

Q. Would you tell me if Westinghouse has any interest in these theses that are being written? A. Well, all these thesis topics are forwarded through my office, at which time they are given a review and forwarded to the Atomic Energy Commission for their review.

Q. What is the purpose of your review of these thesis topics? A. We seek to determine whether they are of general interest to the Bettis Laboratory in the Naval Reactors Work Program.

Q. Do you write a memorandum regarding the decision you make? A. There is a transmittal letter on each application for leave when it is transmitted to the Commis-

sion, which comments on the relevance of this thesis to the Work Program of the Laboratory. This became effective July 1, 1960.

Q. What is the Work Program in the Laboratory? A. It is in the field of nuclear engineering as related to the pressurized water reactor program of the Naval Reactors Program.

[229] Q. And, is it your testimony that all theses have to be in that same general area? A. We try to determine if there is a relationship, although it may be very general in nature. And, if so, we make a comment to that effect.

Q. Now, after you transmit your recommendation to the Atomic Energy Commission, do you receive anything back from them, as a reply, for instance? A. Yes. The man may not initiate his leave until we have a formal approval letter from the Atomic Energy Commission.

Q. Have any thesis been disapproved? A. Yes, they have.

Q. Now, sir, can you tell me if a participant in the Doctoral and Fellowship Program must be an employee of Westinghouse? A. He must be an employee of the Bettis Atomic Power Laboratory at Westinghouse.

Q. And, is this program open to all employees of the Bettis Atomic Power Laboratory? A. It is if they qualify under the conditions that I stated.

Q. How many people do qualify? A. Well, this would require a little bit of explanation. Because, we

[230] have a limited number of slots or positions available on this program each year, and we therefore are forced to impose a competitive type of condition where we may have many more people apply than what we can take because of our shortage of positions being available.

Q. And, what are your criteria once you do select? A. It is the ones which our selection committee feels are the most qualified. But, they must meet the minimum conditions first.

Q. Do participants in the program have any obligation to Westinghouse? A. Prior to July 1, 1960 each participant initiating leave was advised that he was expected to return

to the employ of Westinghouse for a period equivalent to the length of his full time leave.

Q. Did each one return? A. No.

Q. Some left? A. That is correct.

Q. How many? A. Five.

Q. And then, what did Westinghouse do if any-
[231] thing? Or, what did Bettis do? A. Well, as a result of subsequent negotiations between Westinghouse and the Atomic Energy Commission, the program was changed effective July 1, 1960. And, one of the changes was to institute a period of obligation which was effected by a two-year agreement in which they agreed to return to the employ of Westinghouse.

Q. Sir, can you tell us how the Committee decides how much of a stipend will be paid to the participants? A. The stipend is a fixed amount based upon the marital status and the salary of the employee.

Q. It is a percentage of what? A. Prior to July 1, 1960, it was a percentage of his gross salary.

Q. And, afterwards? A. It was an amount determined by the people who are responsible for the program in negotiations with the Atomic Energy Commission.

Q. Was it also based upon the marital status? A. Yes.

Q. And, dependency? A. Right.

Q. And, a percentage of salary? A. The percentage of salary clause was still used. It was still there
[232] technically, but it was never used because the man's salary was always in excess of that amount.

Q. What you did in effect, sir, was to limit the total, is that correct? A. That is correct.

Q. Now, sir, do you know if any other Westinghouse Company benefits are retained by employees while they are on educational leave? A. They receive—or are eligible for—all employee benefits that they had at the time that they initiated their leave.

Q. Could you describe some of those benefits? A. They retain their hospitalization and their pension plan privileges. They are eligible for vacation immediately upon return from their leave. And, they are eligible to participate in the stock option plan.

[234]

Mr. Arkin: Your Honor, we offer these into evidence, Defendant's Exhibits 6, 7, 8 and 9.

Mr. Larrimer: We object on the grounds that this stuff is completely irrelevant to the issue involved. He has already testified these people were eligible for these plans. What is the sense of having the plans themselves in? They don't mean anything. They don't add anything to the issue before the jury and the Court.

The Court: The objection is overruled. Let them be admitted.

[235]

Q. All right. Let us discuss the Plaintiffs individually. Do you know whether or not the Plaintiffs procured the approval of the Bettis Atomic Power Laboratory for these thesis proposals? A. Well, the procedure on the thesis proposals is the man submits an application for educational leave. And, on this application he has a description of his thesis proposal and also a cover memorandum which is signed by his major advisor and by the head of the department in which he is participating at the University.

This is forwarded to us to advise us that this topic, which is described in his application for leave, has the concurrence of the Department and they are willing for him to undertake this topic.

Upon our receipt of this, we add this as a part of a letter to the Atomic Energy Commission to obtain ap-

[236] proval of the funds for this man's specific leave.

Q. Now, when you say "Approval of the funds for this man's specific leave", would you explain that, sir? A. Well, this is part of our agreement with the Atomic Energy Commission, that prior to the initiation of a leave of any individual on the Fellowship Program, we must submit to them evidence that he has qualified—or that he is qualified—for this leave and he is in a position to utilize this leave and has a topic which he can pursue.

Upon their receipt of this, they will advise us of whether these funds will be approved for this purpose.

Q. Then, what you are saying is that there are three approvals; the department head at the University, your approval or your committee's approval, and the Atomic Energy Commission's approval? A. Yes. There are three steps in the chain.

Q. And, the funds come from the Atomic Energy Commission? A. A portion of the funds come from the Atomic Energy Commission. A majority of the funds do.

Q. What portion in 1961 was this? A. Well, there has been various revisions in the funding aspect of this program. And, each one of these men comes under a different set.

[237] Q. During the period in issue, during 1960 and 1961, do you remember what it was? A. Well, Mr. Wolfe's leave was supported entirely by the Atomic Energy Commission until July 1, 1960, After July 1, 1960, the Department of Defense came out with what is called the Armed Services Procurement Regulations which prevented the United States Navy from paying part of this cost, which they had shared with the Atomic Energy Commission at our site. And, therefore, Westinghouse picked up that portion.

For Mr. Johnson, the Atomic Energy Commission paid $420 a month of his leave, and Westinghouse paid $210 a month.

For Mr. Pomerantz, the AEC paid 84.23 per cent and Westinghouse paid 15.77 per cent during the majority of his leave.

Q. Now, sir, you have heard testimony regarding Plaintiffs' Exhibits 1 and 2, which are the statement of purpose and regulations of the Westinghouse Bettis Atomic Power Laboratory Doctoral and Fellowship Programs. Have you not heard such testimony? A. Yes.

Q. Do you as administrator adhere to those regulations? A. Yes, as nearly as possible.

[238] Q. Now, when you say "As nearly as possible", could you explain that? A. Well, the regulations are written as ideally as possible. We live in a world where things do not always work out to the Nth degree of the way we propose them.

Therefore, we try to administer the program as nearly to the regulations as possible. On occasions there have

been exceptions made because of the conditions that existed at that time.

Q. These regulations are really your constitution? A. That is right.

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Cross-Examination

By Mr. Larrimer:

Q. There has been a lot of emphasis by Mr. Arkin on the fact that these benefits are available to employees. Nobody has really gotten into the idea of what is an employee, or who is an employee.

Would you consider that these Plaintiffs were employees of Westinghouse during their leave phase? A. Yes.

Q. And, what is your reason? A. Well, the income which they received and the manpower allocation which was charged against the budget in our department during this period of time.

[239] Q. You are talking about a bookkeeping entry? A. Well, it is more severe than that at our location.

Q. You are talking about an accounting entry of how their stipend was charged? A. Also at our laboratory there is a certain number of employees which we are allowed to have on the rolls at any one time. These individuals are counted against that number.

Q. And, you are talking about another self-imposed restriction at Westinghouse? A. That is correct.

Q. Notwithstanding, during this leave period nobody from your department ever attempted to control the activities of these men while they were on leave, isn't that true? A. Well, at the time they initiated their leave, it was initiated with the understanding that they were to participate in a certain activity at a certain location for a certain period of time.

Q. They were to study for their PhD degrees at the universities and to write a thesis, were they not? A. That is correct, on a subject which we had reviewed.

Q. And, they had to meet the requirements of the universities? A. That is correct.

Q. So, you would say then that all of these
[240] Plaintiffs—Pomerantz, Johnson and Wolfe—were at an educational institution during this leave period? A. They were in educational institutions.

Q. And, they received an amount of money from Westinghouse? A. They received an amount of money monthly from Westinghouse.

Q. Which was in the nature of a living allowance? A. Which was in the nature of a stipend, which was agreed to in advance.

Q. Which was in the nature of a living allowance? Isn't that in your regulations? A. The regulation says "Stipend".

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[245]

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ORVAL A. REDHAIR,

called as a witness in behalf of the Defendant and being duly sworn, testified as follows:

Direct Examination

By Mr. Arkin:

Q. Would you state your name? A. Orval A. Redhair.

Q. Mr. Redhair, did you come to this courtroom in response to a subpoena? A. Indirectly, I would say.

Q. Are you the custodian of the payroll records? A. I would say yes, at this laboratory.

Q. At the Westinghouse Bettis Atomic Power Laboratory? A. Right.

Q. Did you bring the records with you? A. I have the records for these three employees for the years 1960, 1961 and 1962.

Q. Are these the records? A. They are in that briefcase.

Q. Using the records to refresh your recollection, sir, can you tell me what account each Plaintiff was
[246] paid from prior to his educational leave? A. Prior to the educational leave of each employee, the employees were paid from the payroll account. And, such payments were charged to direct labor under the contract.

Q. Now, what does that mean, sir? Can you explain that? What is "direct labor under the contract"? A. In our accounting terminology, those charges to direct labor mean that the efforts were identified to a particular project or phase of the operation, and so identified as costs under the contract.

Q. Do I understand you to mean that this would be costs of a particular project? A. They would be costs of a particular project or that phase of the operation which is covered by a specific contract.

Q. Well, would you kindly illustrate what project you mean or what project we are talking about? A. Well, the individuals indicated, I believe, earlier in the record the effort and the type of work that they were doing. There is a particular directive under the contract for the efforts required on each of those types of work.

I am not familiar enough with the terminology of the technical efforts to be able from the records here to say exactly what the efforts were. But, in our [247] accounting terminology, we apply as first costs of an effort direct labor, material and indirect labor. They are your main components.

Q. Now, sir, what accounts were the participants paid from while they were on educational leave? A. While on educational leave, those payments are classified as indirect labor, or overhead.

* * *

Q. Now, explain to us what indirect labor means? [248] A. Indirect labor is absorbed in the cost of a project on a pro rata basis. The direct labor effort is recorded in hours and valued at the going rate and charged against the particular effort.

In addition to that direct labor, of course, there are direct materials and the supplies, and the indirect labor such as supervision, clerical efforts and maintenance or cost of operations.

Items of this nature are included in overhead and recovered on that basis.

Q. Is there an account number for a scholarship or fellowship? A. Not as such.

* * *

Q. Do you know, sir, if deductions were made from the Plaintiff's stipend checks? A. Yes, there were deductions made.

Q. What deductions, and for each particular Plaintiff? A. Well, in general, for all there were income tax deductions made and social security deductions.

And, there were deductions when authorized which were made for dependent coverage under the insurance plan and for a contributory portion of our pension plan.

[249] Q. That is in general. Can you give us a little more specific picture for each? A. I don't have the complete record for all of those items. The deductions for dependency coverage under the insurance plan and for a contributory portion of the pension plan are at the option of the employee and are made only when so authorized.

* * *

[250] Q. Did the Plaintiffs receive any salary increases while they were on educational leave? A. From the records I have here, Messrs. Johnson and Pomerantz had no change in salary while on stipend. There were minor adjustments in Mr. Wolfe's case. And, my recollection of that would be that the cost of living index changes were made quarterly at that time.

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[251]

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WILLIAM F. MAHER,

called as a witness in behalf of the Defendant and being duly sworn, testified as follows:

Direct Examination

By Mr. Arkin:

Q. Would you state your name? A. William Francis Maher.

[252] Q. Mr. Maher, did you come here in response to a subpoena? A. Yes, sir, I did.

Q. What is your occupation, sir? A. I am assistant manager of industrial relations for the Bettis Atomic Power Laboratory, Westinghouse Electric Corporation.

Q. As one of your duties, do you keep the personnel files of the Plaintiffs? A. Yes. They are under my jurisdiction.

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[253]

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Q. Well, when Dr. Pomerantz went on educational leave, did this affect in any way his seniority status or accrued service status? A. No, sir, not under the Fellowship Program.

Q. It did not affect it? A. No, sir.

Q. Can you tell me when Mr. Wolfe entered on duty? A. 8/20/52. That is August 20, 1952.

Q. Now, for the period while he was on educational leave, was there an adjustment made for his absence in terms of his seniority status? A. No, sir.

[254] Q. Can you tell me what date Mr. Johnson entered on duty? A. June 18, 1956. He was again a Westinghouse Electric Corporation graduate student. And, this is the corporation date. His accredited service date with the corporation dates from 6/18/56.

Now, he transferred to the Bettis Atomic Power Laboratory on July 2, 1956, according to his records.

Q. Now, again, sir, was there some change while he was absent on educational leave in his accredited service or seniority status? A. No, sir.

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[255]

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MARTIN A. DAUGHERTY,

called as a witness in behalf of the Defendant and being duly sworn, testified as follows:

Direct Examination

By Mr. Arkin:

Q. Would you state your name? A. Martin Aloysius Daugherty.

Q. Where do you live, Mr. Daugherty? A. 5435 Wolfe Drive, Pittsburgh 36.

Q. And, by whom are you employed, sir? A. United States Atomic Energy Commission at the Pittsburgh Naval Reactors Office.

Q. Could you tell us what your position is there? A. The title of the job is director, organizational personnel division.

Q. What does the title mean? A. Sometimes not very much. The functional duties ascribed to the job are that I am responsible to plan, direct and administer a program for the accomplishment of federal personnel programs, organization management, the administra-
[256] tion of contractor personnel activities, records management, communications, and several other house services.

With regard to the specifics here in the contractor personnel phase, I have the responsibility to administer the entire contractor personnel program to include the recruitment, training, job evaluation, staffing, et cetera.

Q. When you refer to "contractor personnel", to whom are you referring? A. The Westinghouse Electric Corporation at the Bettis Atomic Power Laboratory. Now, if I may take a minute to explain—

Q. Go ahead. A. The site of the Bettis Atomic Power Laboratory, for all practical purposes, is completely owned by the Government. That is, all the plant and equipment and facilities.

It is operated under a contract with the Atomic Energy Commission, and it is funded primarily through the Atomic Energy Commission's funds, although there are some navy dollars involved in it.

Q. Is what you are saying that the Government owns the plant and Westinghouse runs it? A. Yes, sir. It is commonly known as a Government-owned contractor-operated plant.

Q. Does Westinghouse, to your knowledge, do any other work besides work for the Government at
[257] this plant? A. To the best of my knowledge, no.

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[258]

Q. Does Westinghouse make the expenditures first and then they are reimbursed, or do they seek prior approval? A. Well, it depends on the set of circumstances. It is not a simple proposition. There is some advance funding —for instance, in the banks—for the payroll. That is for that portion of it.

Primarily and basically, we follow a post-audit review, at which time adjustments are made to actual spending. There is further under the cost-type setup a provision where there is no risk to the contractor and a series of reviews are made, or proposals, for the contractor to perform certain actions. In certain instances of this kind, the contract in part requires a prior approval from the contracting officer.

Q. Can you tell me what sore of items require prior approval? A. Yes, sir, I can. And, may I use an example.

One contract article provides that any salary in excess of a certain amount shall be submitted to us on an individual basis for approval. And, we in turn then have to submit this to AEC headquarters.

[259] There is an approval requirement in this particular relationship. The individual young men, prior to their going on their doctoral leave or educational leave, must comply with this.

There are other approvals in there that vary considerably.

Q. You stated that each individual participant in the Doctoral Program had to have prior approval before he could go on educational leave? A. Yes, sir.

Q. Does that apply to the whole program? A. Well, the program is basically approved. Can I start at the beginning and explain this?

Q. Certainly. A. In the construction of the records, I was not here. I was employed at the Pittsburgh Reactors Office in 1958 in September.

The program was new to Westinghouse. It was submitted to the AEC for approval. And, the AEC did approve it, with limitations.

Then, one of the limitations was that when the individuals involved went on leave, that they would be approved on an individual basis by the Atomic Energy Commission.

[260]

Wednesday Morning,
November 23, 1966.
Jury Present.

[269]

Q. Now, I think, Mr. Daugherty, when we left off yesterday I had asked you a question. We talked about the Bettis Doctoral Program, and I think my question was what was the basis for the Atomic Energy Commission's approval of that program.

[270]

The Witness: May I refresh myself just a minute?

Q. Did you bring your personnel files with you? A. Yes, I have them. Excuse me a minute.

(Interval)

In 1955, there were discussions between the Atomic Energy Commission and Westinghouse, which led to such a program.

In mid-year—maybe in the fall of the year
[271] or late summer—Westinghouse advised the Atomic Energy Commission that such a program was in the offing, and laid out certain details of it.

Later in the year—I think toward the end of the year—Bettis specifically proposed the entire program and requested the Commission to reimburse the costs of the program.

Q. The program was then approved, was it? A. Generally, yes. There were some limitations on it.

Q. Now, is this program, the Doctoral Program at Bettis, in any way related to the Atomic Energy Commission's and the Bettis Laboratory's needs or work products?

[272]

The Witness: Well, the Bettis Laboratory's needs include a need for people—top technical people—capable of operating in complex nuclear technology.

This is part of the reason that the program was created. As Dr. Vogeley testified yesterday, I think it is pretty well established that the program was designed to attract people to the Bettis Laboratory and provide them with an educational opportunity leading to the PhD degree, and to eventually fill the needs for the top technical talent.

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[273]

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Q. Now, you stated that the program was approved by the Atomic Energy Commission. Can you tell me, sir, if you know whether or not the Atomic Energy Commission retained any control during the period in issue, which is 1960, 1961 and 1962, I believe, over specific theses topics chosen by the participants at the Westinghouse Bettis Atomic Power Laboratory? A. Yes, sir. Part of the approval requirement was that Westinghouse submit to the Atomic Energy Commission, prior to the individual going on his educational leave, a recommendation to us that dealt with the general application of the proposed thesis topic to the Bettis work.

Q. When you say "Bettis work", what specifically do you mean? A. Well, the work program, the purpose or the reason that Bettis is in existence. It would cover
[274] the scope of the work defined in the contract between AEC and Westinghouse.

Q. Do you know generally, sir, what the scope of that work is? A. Generally, yes.

Q. Could you tell us? A. It generally involves nuclear engineering, design research and development effort in the Naval Reactors Program, and certain central station reactors. That is, power stations.

Q. And, you testified that the thesis topic must be related to this work done at Bettis as a general rule? A. That is correct.

Q. Now, more specifically, have there been any high-level meetings at which you were present where this problem was discussed? A. Yes. In 1959, I met, together with a man named Richard March of the Atomic Energy Commission, with Westinghouse—and also present were Mr. Richard Cunningham, Mr. Van Horn and Mr. Qninn, who are present here—to discuss the relationship of the theses topics to the fields of work.

One of the specific reasons for doing this was that the Atomic Energy Commission has always believed that a man should have a job relatedness in his training
[275] assignments. And, I believe this is what Mr. Quinn brought out yesterday.

And, we discussed the fact that if a man is to be trained in a specialty, then that specialty should be related to his field of interest and his work assignment or future work assignment.

As I recall, we ended up in agreement on this.

Q. Now, when you review applications for educational leave, sir, is that one of the factors which you consider? A. Yes, sir, in its general application.

Q. Do you make a recommendation? A. Yes, sir. May I tell you the procedure we follow in our own organization?

Q. Certainly. A. The transmittal letter comes over addressed to the contracting officer, who is the manager of the Pittsburgh Naval Reactors Office, and it usually ends up with me.

I am then responsible to properly staff the proposal through our technical people and to arrive at a unanimous decision, and to make a recommendation and endorsement to the manager as to whether the leave should be approved.

Q. In the individual Plaintiffs' cases—and you heard the testimony that they did go on leave and that they did study in certain areas—are you in a position to state whether or not the AEC did approve those par-
[276] ticular Plaintiffs' leaves? Do you recall? A. I recall two of them, but I do not recall Mr. Wolfe, or Dr. Wolfe.

Q. Is it the general practice of your office to review each applicant? A. Yes, sir.

Q. Do you know that that is done? A. Yes, sir.

Q. Have you ever disapproved a thesis topic? A. Yes, sir. We have disapproved them, but we have not formally disapproved them. We have discussed the matter with Westinghouse, and the Bettis people were kind enough to withdraw that specific topic.

Q. Now, is the Doctoral Program reviewed in any way in general by you periodically? A. Yes, and others. Periodically we review it.

There is a requirement—an AEC requirement—that certain reports shall be submitted to headquarters. Bettis complies with this obligation, and we review those reports as they come in. As Dr. Vogeley testified, they are status reports.

In addition to that, we periodically review and evaluate the program. And, annually Bettis proposes a new class, a new number of people, a number of participants, and we try to match and relate the number of PhD's to [277] the Bettis work program and decide on the number of people and whether a new class should be approved.

Q. Do you know, sir, if there is a requirement at Bettis that a certain number of PhD personnel be hired? A. Not to my knowledge, no, sir.

Q. Is the number of PhD personnel at Bettis important in any way? A. You said the number?

Q. Well, in general, yes. A. Well, it is important to AEC's way of thinking that there is a number of PhD's at the Bettis Atomic Power Laboratory. It is certainly very desirable.

* * *

Q. Your statement was that it was important to the Atomic Energy Commission? A. Yes, sir.

Q. In what way? A. It is important to have top technical talent at the laboratory to successfully carry out the mission of the contract.

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[284]

Q. Now, Mr. Daugherty, you have heard testimony, have you not, that two of the Plaintiffs were required to sign documents known as employment agreements? A. Yes, sir.

Q. This was prior to their taking of educational leave? A. Yes, sir.

Q. Do you know how long those agrreements have been a requirement? A. Since 1960.

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Q. Did the Atomic Energy Commission require the formal written agreement?

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The Witness: Yes, sir.

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[285]

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Q. Do you know, sir, if prior to 1960 there was an obligation of any kind to continue working in the employ of Bettis after completion of educational leave? A. Yes, sir. There was an obligation referred to sometimes as a moral obligation to return for one year after completion of the leave period.

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Q. Mr. Daugherty, was this Doctoral Program, and specifically the studies of each individual in the Doctoral Program, incident to the contract work of the Westinghouse Bettis Atomic Power Laboratory?

* * *

The Witness: We considered it so, as an obligation to reimburse the costs as a personnel expenditure.

The Appendix A which references this specific program has a statement that to meet the contract needs
[288] there are certain educational programs included in it as a Fellowship Program.

* * *

Q. Now, Mr. Daugherty, if you know, will you tell us specifically whether or not the costs of research and development of Westinghouse are such "costs"? Do you understand me? A. No, I don't understand you, sir.

Q. I am referring to Article 10 of the contract which you are generally familiar with, are you not? A. Yes, sir.

Q. Now, to specifically tie this down, you have stated that the payments to the individuals under the Doctoral Program were incident to the contract, is that right? A. Yes, sir.

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[289]

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Q. You have testified, sir, that Westinghouse has specific contract commitments, is that right? A. Yes, sir.

Q. And, those contract commitments are for research and development into nuclear power projects? A. Gen-

erally in the Naval Nuclear Reactors Program, yes, sir.

Q. Now, the question I am trying to ask is if the payments to each individual recipient are directly attributable to the contract commitments of Westinghouse to

[290] the Atomic Energy Commission? A. There is an obligation in the commitment by the Government to reimburse Westinghouse for costs of its personnel expenditures. There is a further obligation and a commitment by the Government to reimburse to Westinghouse all costs that are reasonable and incurred necessary and incident to the work that is performed under the contract.

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[291] Cross-Examination

By Mr. Larrimer:

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[293]

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Q. Now, one of the requirements, I believe you stated, was that the thesis topic be approved by AEC? A. Yes, sir.

Q. And, I think one of the reasons, is it not, is that the topic itself be publishable? In other words, it is not what we call classified information? A. Well, that is a second step. That didn't come into our consideration here on the approval, or on the approval requirements. What we wanted to assure ourselves of was that the training had general application to the laboratory's work effort.

Q. A general application? A. Yes, sir.

Q. Now, you are not an engineer, are you, Mr. Daugherty? A. No, sir.

Q. And, you can't give us any limitations on the use of the word "general application"? A. I don't understand you.

Q. Well, what I am asking you, is it not true that the thesis topic must be in an engineering field? A.

[294] Yes, sir, if the man is in the reactor engineering portion of it.

Q. And, isn't it true—if you know—that practically any additional information in the engineering field would be related to the work at Bettis?

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[295]

Q. Well, I suppose since we have gotten into this area of what the contract between the Atomic Energy Commission and Westinghouse provides, and the categories of the costs, that I should ask you this question. Was the AEC aware of this program by which these men were securing these degrees? A. Yes, sir.

Q. And, did it approve of these, and of this program? A. Yes, sir.

Q. And, the AEC, of course, knew that these people secured a PhD degree from a university? A. Yes, sir. There is a requirement, as you mentioned earlier, that the approval be submitted to us, or requested of us, to go on the leave.

Q. And, your Commission also knew that during this leave of absence period that these men had no activities at all at your Bettis plant? I mean, no work activities? A. Yes, sir.

[296]

Q. You knew that this was a strict leave of absence and this stipend was paid to them during this period? A. As a leave of absence, yes.

Q. So that, there is nothing to indicate that anybody exceeded their authority? We are not trying to establish any excess of authority, are we? A. No, sir. The only thing I can recall, if I might add, sir, is that the reports that were submitted to Dr. Vogeley were status reports. Now, I don't know if that would have any bearing on your question as to work activities.

Redirect Examination

By Mr. Arkin:

Q. Mr. Daugherty, does anybody else review these leave applications besides yourself? A. Yes, sir. I testified that I staff them through our technical people.

[297]

JOHN R. VAN HORN,

called as a witness in behalf of the Defendant and being duly sworn, testified as follows:

Direct Examination

By Mr. Arkin:

Q. Mr. Van Horn, where do you live, sir? A. 5497 Library Road, Bethel Park, Pennsylvania.

Q. And, by whom are you employed? A. Westinghouse Electric Corporation.

* * *

Q. How long have you been employed by Westinghouse? A. I was first employed in 1950, in July. I continued in their employment until the end of 1961. And, I returned to Westinghouse in April of this year.

Q. What is your position? A. Administrator, engineering, training and development, training development department.

[298] Q. Is that the overall Westinghouse Electric Corporation? A. Yes, it is.

Q. Were you at any time more specifically involved in the Bettis Atomic Power Laboratory? A. Yes.

Q. When was that, sir? A. I was at the Bettis Atomic Power Laboratory from my initial employment in 1950 through May of 1961.

Q. What was your capacity or your occupation at Bettis? A. I was originally employed as assistant to the director of research, and subsequently assistant to the director of development.

And then, in the fall of 1954, I was staff assistant to the assistant to the division manager of the Atomic Power Division. I continued in that capacity until July of 1955, at which time I became director of education and training at Bettis.

Subsequently, I was made manager of education and training, which position I continued until I left Bettis in May of 1961.

Q. Now, as director and then manager of education and training, what did you do? A. Well, I had re-

[298] sponsibility for education and training programs, both technical and non-technical, involving West-

inghouse programs as well as programs associated with the universities.

More specifically, I had under my responsibility the Bettis Doctoral Fellowship Programs.

Q. Do you remember, sir, when the Bettis Doctoral Programs were established? A. Yes.

* * * *

Q. * * * at the time the Bettis Doctoral Programs
[300] were established, why were they established? A. Well, of course, at the time—and this was in the spring of 1955—I was staff assistant to the division manager's assistant, and the man to whom I reported was concerned with it.

Mr. Larrimer: This is hearsay evidence, and I object to it.

The Court: Doctor, if you know why the program was established, you may say. If you don't know, you may not say. Don't tell us what anybody told you.

The Witness: All right. The program was established because there was a need to attract qualified young graduates in engineering. And, this was an aid in attracting these individuals to come to the employment at Bettis and work in the work program.

Also, it was to upgrade their technical confidence so they would be able to perform at a high technical level.

By Mr. Arkin:

Q. Now, sir, do you know why it was necessary to bring young technical people to Bettis and upgrade their performance at this period? A. Well, the laboratory at that time had increased demands for people to fulfill the contractual requirements to the Atomic Energy Commission.

And, as far as the quality and numbers of people
[301] that could be attracted, it was felt that by offering such a program as this that we could augment the attractiveness and augment the numbers of people we could obtain.

Q. In other words, you felt you could bring people in with this program, is that right? A. That we might not otherwise be able to attract, yes.

Q. I see. And, you said there was an increased demand for people to augment contractual requirments to the

Atomic Energy Commission? Is that a fair statement of what you said? A. Yes, I think so.

Q. Were these contractual demands any different at that time than they had been previously? A. I don't know whether this question implies that I am familiar with the contractual demands or the details of the contract. If so, it would not be possible for me to testify on that matter.

Q. What I am asking you, sir, is do you know if or whether or not at that time there were more projects suddenly assigned to Bettis for which you had to find people to staff? A. Yes. As I recall, that was the case.

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Q. Mr. Van Horn, do you know whether in fact your purpose was in fact accomplished? Did you attract personnel? A. Yes.

Q. Were you able to fulfill your Atomic Energy Commission requirements? A. Well, I don't know that I know all the requirements.

Q. Well, as best you can answer that? A. Through this program?

Q. Did this program aid you? A. It helped, yes.

[303] Q. Significantly, or not? A. Yes.

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Cross-Examination

By Mr. Larrimer:

Q. Mr. Van Horn, then the primary purpose of this whole program was to attract personnel to Westinghouse at Bettis, is that true? A. I would certainly say that one of the objectives was to attract qualified individuals.

Q. You don't want to label it "primary", but that was one of the principal objectives? A. Yes.

Q. To attract personnel? A. Sure.

Q. Now, you have indicated, and you have attached the label to this program as "Attractive". How was this program attractive to people who would be in a position of the Plaintiffs? A. Well, I think it would be attractive, and it was attractive in the sense of providing an opportunity for them to attain additional education, which

would enable them to work at a higher level or at a more sophisticated level or technical level.

[304] They also would have the opportunity in their work experience with the laboratory to gain experience working with high-level people.

Q. But, the attractive feature of this was the educational benefit, is that right? A. The educational benefit and, I also might add, the opportunity to work in an interesting field with rather high-level competent individuals.

Q. I am talking about the Doctoral Program itself. I am not talking about the job that you hoped these men would take. It was strictly an educational opportunity that was the attraction, is that true? A. Well, I think that in our brochures and so on that were put out to attract these people, we also indicated not only the educational opportunities but also the opportunity to work in a new and exciting field with very competent technical people.

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[305] Mr. Arkin: Now, Your Honor, comes now the Defendant at the close of the Defendant's case and renews its motion for a directed verdict—

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Mr. Arkin: Let me, for purposes of the record, move for the directed verdict on the same grounds and for the same reasons which I moved at the close of the Plaintiffs' case.

The Court: All right. And, the motion is denied. The Court thinks the question is for the jury.

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WILLIAM A. QUINN,

having been previously sworn as a witness, was recalled in behalf of the Plaintiffs and testified further as follows:

Direct Examination

By Mr. Larrimer:

Q. Mr. Quinn, I believe it was brought out on direct examination by the Government that you are familiar with

the payments made to these men during their
[313] leaves of absence? A. Yes, that is right.

Q. And, I believe you testified that Westinghouse withheld taxes? A. Yes.

Q. Commonly designated as withholding taxes? A. That is correct. They were withheld from the stipend payments.

Q. Now, during this same period, during the period that these men were on their respective leaves of absence, is it not true that Westinghouse also paid their tuition? A. That is correct. They paid the tuition and fees.

Q. And, the fees to the schools? A. The amounts were reimbursed to the individuals, not to the schools.

Q. These were paid to the individuals? A. That is correct.

Q. And, was withholding tax withheld from these amounts? A. No. The reimbursement was made in the form of cash through our petty cash fund.

Q. Very good. Now, this was all part of the Doctoral Program? A. That is correct.

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[314]

Cross-Examination

By Mr. Arkin:

Q. Mr. Quinn, what you are saying is that there was a determination made by Westinghouse to withhold taxes on the stipends but not to withhold on the tuition payments? A. Yes. This determination was on the advice of our tax counsel.

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[315]

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RICHARD E. JOHNSON,

having been previously sworn, was recalled in behalf of the Plaintiffs and testified further as follows:

Redirect Examination

By Mr. Larrimer:

Q. Your project, Mr. Johnson, during your leave of absence was what? A. The study of the effect of hydrogen on the internal friction of zirconium metal.

Q. Well, you did not complete this project? A. I did not.

Q. And, did you continue in your employ at Westinghouse then after your leave of absence? A. Yes, sir.

Q. When did you leave Westinghouse? A. The spring of this year.

[316] Q. That would be 1966? A. Yes.

Q. And, to your knowledge, did Westinghouse after you had abandoned this project pick it up to try to get the answer that you were seeking? A. To the best of my knowledge, sir, neither the Bettis Laboratory nor any other branch or division of the Westinghouse Electric Corporation has pursued this subject. Nor, to the best of my knowledge, has anyone else in this country pursued this subject.

And, furthermore, may I say and may I go on the record as saying that it is my intention eventually to carry this experiment to a successful completion for its academic and scientific interest.

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Mr. Arkin: Your Honor, now at the close of all the evidence, the Defendant renews its motion for a directed verdict on the same grounds as it stated in its motion at the close of the Plaintiffs' evidence and at the close of the Defendant's evidence.

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The Court: Oh, I think that is very well demonstrated by the cases you cited—about ten of them in this country—where learned judges disagreed. There is no rule that I can put my finger on that would decide this case. People find facts differently where there is room for disagreement. And, obviously that is why the judges disagreed.

That is also why we must submit this case to the jury. There is a fact question here for the jury of whether this was a scholarship excludable from gross income or whether it was not.

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[375]

The Court: Your brief argued that I should direct a verdict for the plaintiffs.

Mr. Larrimer: Well, I understand you cannot direct a verdict for the plaintiffs.

[377] Monday Morning, November 28, 1966.

[420] CHARGE OF THE COURT

The Court: Members of the jury, as you know, this lawsuit was brought by the Plaintiffs Doctors Johnson, Pomerantz and Wolfe and their wives to recover income taxes from the Defendant the Director of Internal Revenue, which taxes the Plaintiffs contend were illegally and erroneously assessed and collected by the Defendant on payments of money, or stipends, which they received from Westinghouse during the periods they were on educational leave from their employment with Westinghouse in order to pursue studies and research as candidates for degrees of Doctor of Philosophy.

[423]

In order to arrive at the truth, you must necessarily determine the facts and draw the reasonable and proper inferences from the testimony and the circumstances. This duty requires you to pass upon the credibility—that is the believability—of each witness.

You judge the credibility of a witness by the manner in which he gives testimony from the witness stand, his demeanor on the stand, the reasonableness or unreasonableness of his testimony, his means of knowledge about what he testifies, his interest in the outcome of the case if any, and any circumstances tending to shed light upon the truth or falsity of such testimony.

And, it is for you to say what weight you will give the testimony of each witness. Although you are to consider

only the evidence, you are not limited to accepting the bald statements of witnesses. On the contrary, you may draw from the facts you find proved such reasonable inferences as seem justified from the evidence in the lgiht of your own experiences.

In deciding what weight you will give the testimony of any witness, you may use that common sense, judgment and experience which you use in your everyday activities.

[424] Where facts are in dispute, it is your duty to reconcile the evidence if possible. If you cannot reconcile the evidence, it is your duty to determine which witnesses you will believe and where the truth lies.

There is very little evidence in dispute in this case. As I recall, the only major dispute involves whether or not the research projects undertaken by the Plaintiffs while on educational leave at the universities were services performed by the Plaintiffs for Westinghouse which were subject to the control and supervision of Westinghouse. The Plaintiffs want you to believe they were not; the Defendant wants you to believe they were.

Now, the pertinent provisions of the Internal Revenue Code—and this is only one of about ten books—provide as follows. This is known as Section 61. It defines gross income. A general definition of gross income is as follows.

Except as otherwise provided, gross income means all income from whatever source derived, including the following items; compensation for services like wages and salaries, other items like gross income from business, gains derived from dealings in property where you sell a house and you get a nice gain over what you paid for it, interest, rents, royalties, dividends, and many others.

[425] You will note that compensation for services —and that is payments for work done or services rendered—to a company are to be included in gross income. Under the law, such compensation must be reported in the taxpayer's income tax return as gross income, and income taxes paid thereon.

One of the important issues in this case is whether or not the stipend received by each Plaintiff from Westinghouse while on educational leave was compensation for employment services rendered to Westinghouse.

Now, the definition of gross income plainly indicates that there are exceptions to what is meant by "gross income". The definition states, "Except as otherwise provided".

Now, Section 117 of the Code specifies an exception. This exception is called a scholarship or fellowship grant. Scholarships or fellowship grants generally consist of money received by a student from some grantor to enable the student to pursue studies or research at a place of learning such as a university.

That money received by the student is not to be included in gross income. That money—or stipend as it has been called in this case—is excluded from gross income and need not be reported in the student's income tax return. Or, if it is reported, he need not pay a tax on it.

[426] If by chance income taxes are illegally and erroneously assessed and collected on that scholarship money, or stipend, the student is entitled to have the taxes so collected returned to him. We call that a refund.

The Plaintiffs are suing for refunds of the taxes assessed and collected on the stipends they received from Westinghouse while they were on educational leave. The Plaintiffs contend those taxes were illegally and erroneously assessed and collected on the stipends because the stipends were scholarships. The Defendant contends that the taxes were legally assessed and collected and should not be returned to the Plaintiffs.

Now, I shall read the pertinent parts of Section 117. Section 117 provides the general rule, in the case of an individual, gross income does not include, one, any amount received as a scholarship at an educational institution or as a fellowship grant.

A scholarship may be defined as follows. A scholarship generally means an amount paid or allowed to, or for the benefit of, a student, whether an undergraduate or graduate, to aid such individual in pursuing his studies.

The term includes the amount of tuition, matriculation and other fees which are furnished or remitted to a student to aid him in pursuing his studies.

The term also includes any amount received in the nature of a family allowance as a part of a scholarship.

[427] A fellowship grant may be defined as follows.

A fellowship grant generally means an amount paid or allowed to, or for the benefit of, an individual to aid him in the pursuit of study or research.

The term includes the amount of tuition, matriculation and other fees which are furnished or remitted to an individual to aid him in the pursuit of study or research.

The term also includes any amount received in the nature of a family allowance as a part of a fellowship grant.

Now, for the purposes of this case, a scholarship and a fellowship grant are substantially the same.

A candidate for a degree may be defined as follows. The term "Candidate for a degree" means an individual, whether an undergraduate or a graduate, who is pursuing studies or conducting research to meet the requirements for an academic or professional degree conferred by colleges or universities.

A student who receives a scholarship for study at a secondary school or other educational institution is considered to be a candidate for a degree.

The Plaintiffs Johnson, Pomerantz and Wolfe contend that the payments or stipends each received from Westinghouse while on educational leave at the University of Pittsburgs or Carnegie Institute of Technology were excludable from gross income because each received these

[428] amounts as a scholarship at an educational institution.

Therefore, the ultimate questions of fact which you are to decide from the evidence are, first, were the amounts received by Richard E. Johnson from Westinghouse a scholarship at an educational institution excludable from his gross income. And, you will answer the question yes or no.

The second question is the same; were the amounts received by Martin L. Pomerantz from Westinghouse a scholarship at an educational institution excludable from his gross income. And, you will answer yes or no.

Third, were the amounts received by Richard A. Wolfe from Westinghouse a scholarship at an educational institution excludable from his gross income. And, you will answer yes or no.

The question could just as well have read, was the stipend received by a Plaintiff a scholarship or a fellowship grant. But, as I have said, the words "amounts received" have the same meaning as "stipends received". And, the designation "scholarship" has the same meaning as "fellowship grant". Or, at least, it has substantially the same meaning.

You are instructed that amounts of money or stipends paid to an individual to enable him to pursue studies or research are considered to be amounts received as a scholarship or fellowship grant if the primary purpose of
[429] the studies or research is to further the education and training of the recipient in his individual capacity and the amount provided by the grantor for such purpose does not represent compensation or payment for employment services to the grantor or services under the grantors' direction or supervision.

If the primary purpose of the studies and research is to further the education and training of the recipient in his individual capacity, neither the fact that the recipient is required to furnish reports of his progress to the grantor nor the fact that the results of the study or research may be of some incidental benefit to the grantor shall of itself be considered to destroy the essential character of such amount or stipend as a scholarship or fellowship grant.

You are further instructed that, one, any amount of money paid to an individual to enable him to pursue studies or research, if such amount represents either compensation for past, present or future employment services, or represents payment for services which are subject to the direction or supervision of the grantor, then the amount paid to the individual is not a scholarship or fellowship under the tax laws.

Two, any amount of money paid to an individual to enable him to pursue studies or research which studies or research are primarily for the benefit of the
[430] grantor is not a scholarship under the tax laws.

[431] • • •

The evidence you should consider with respect to the nature of these payments the Plaintiffs received from Westinghouse to enable them to pursue their studies or research is the testimony relating to the basis of fixing the amounts

of the stipends which the Plaintiffs received while on leave.

There was testimony that the stipends were fixed on a percentage of their salaries plus adders for dependents, with a fixed maximum amount.

You should consider the evidence relating to the source of the money paid to the Plaintiffs while on leave.

You should consider the evidence relating to the coverage of Plaintiffs by Westinghouse employee plans for vacation, retirement, sick leave, stock options, and
[432] perhaps employee benefit plans while they were on leave, and evidence relating to their accredited service or seniority.

You should also consider the evidence that Westinghouse withheld income taxes and social security taxes from the stipends paid to the Plaintiffs during their leaves, and deducted from the stipends assessments for pensions and insurance when authorized by the employee.

In this connection, you should also consider the evidence that Westinghouse did not withhold income taxes or social security taxes from the tuition which Westinghouse paid to the Plaintiffs to enable them to attend the universities.

I am sure you all know that all universities require their students to pay tuition for their studies and research at the universities.

Were these payments compensation for services to Westinghouse or were they amounts received in the nature of a family allowance as part of a scholarship? The Plaintiffs contend they were part of a scholarship; the Defendant contends they were compensation.

With respect to the purpose of the studies and research, you should consider the evidence relating to the need of the Bettis Laboratory of Westinghouse for PhD personnel, or Doctor of Philosophy personnel.

You should consider the evidence that each Plaintiff spent his leave engaging in studies and research in
[433] laboratories at the universities, and prepared a thesis in order to secure a degree of Doctor of Philosophy. There was not evidence that any Plaintiff did any work or performed any duties at the Bettis Laboratory, or at any other Westinghouse plant, during his leave.

You should consider the evidence relating to the thesis topics which were undertaken and written; to whom the theses were submitted after they were written; the oral

presentation of the theses; and, where the oral presentations were made, who was present, who examined and questioned the Plaintiffs, who voted to accept the theses, where they were published, where they were kept, to whom they were available for reading, who benefitted from these theses, and other testimony in this respect.

Was the primary purpose of the studies and research to further each Plaintiff's training and education as an individual, or were the studies and research primarily for the benefit of Westinghouse?

With respect to whether Westinghouse or the universities had supervision and control of the research projects the Plaintiffs pursued while on educational leave, the Plaintiffs want you to believe from their evidence that the research projects they participated in at the universities were not under the control or supervision of Westinghouse,

[434] but were exclusively under the supervision and control of the universities and their respective faculty advisors. that Westinghouse imposed no restrictions on the universities or on the faculty advisors with respect to the research projects; and that the research projects the Plaintiffs engaged in while on leave were not services performed for Westinghouse.

On the other hand, the Defendant wants you to believe that the research projects engaged in by the Plaintiffs while on leave were services performed for Westinghouse and that those research projects and services were under the supervision and control of Westinghouse. On this issue of fact, you will have to determine which witnesses you will believe in the light of all the facts and circumstances in the case.

You should consider the evidence relating to how these topics were selected and who approved them. There was evidence that these topics were approved by the faculty advisors, by the university committees, by Westinghouse, and by the Atomic Energy Commission.

All these factors, and others that I may not have mentioned, should be considered by you in arriving at the facts. The weight to be given each factor is entirely for you.

Now, each Plaintiff wants you to believe that the primary purpose of his studies and research at the university while on leave from his employment with Westinghouse was to

further his education and training in his individual capacity.

In other words, each Plaintiff wants you to
[435] believe that the primary purpose of the studies or research was to benefit him in his personal status or character as an individual by additional education and training in order to obtain a degree of Doctor of Philosophy.

If you find this to be the fact by a fair preponderance of the evidence and the reasonable inferences to be drawn therefrom, then the amount or stipend paid to him by Westinghouse during his educational leave to pursue studies and research was received by him as a scholarship excludable from gross income.

In this connection, I instruct you that the fact that each Plaintiff was required to furnish progress reports to Westinghouse does not of itself destroy the essential character of the stipend as a scholarship.

And, I also instruct you that the fact that the results of a Plaintiff's studies or research may be of some incidental benefit to Westinghouse likewise of itself would not destroy the essential character of the stipend as a scholarship.

Thus, if you find the stipend received by a Plaintiff to be a scholarship excludable from gross income, the assessment of income tax on that stipend was illegal and erroneous, and such Plaintiff is entitled to a refund.

If you so find the facts, your answer to the appropriate question should be yes. On the other hand, if you
[436] find from the evidence and the reasonable inferences to be drawn therefrom that the studies and research pursued by a Plaintiff at Pitt or Tech were primarily for the benefit of Westinghouse, then in that event the amount or stipend paid to him is not an amount received as a scholarship.

If you find this to be the fact, then the assessment of income taxes on the stipend was legal and proper under the law and such Plaintiff is not entitled to a refund. Therefore you would answer the appropriate question no.

Also, if you find from the evidence and the reasonable inferences to be drawn therefrom, one, that the stipend paid to a Plaintiff to enable him to pursue his studies and research compensation for employment services performed by such Plaintiff for Westinghouse before the educational

leave began, or, two, if you find the stipend represents compensation for employment services performed by such Plaintiff for Westinghouse after the educational leave ended, or, three, if you find that the stipend represents compensation for employment services performed by said Plaintiff for Westinghouse while on educational leave, or, four, if the stipend represents payment for services performed by such Plaintiff for Westinghouse which were subject to the direction or supervision of Westinghouse, then any one of these findings will require you to conclude that the amounts of money or stipends so paid to

[437] a Plaintiff were not amounts received as a scholarship.

In short, if you find from the evidence that the stipend received by any Plaintiff from Westinghouse represents compensation for employment services rendered to Westinghouse or services subject to the direction and control of Westinghouse, then such Plaintiff is not entitled to a refund and you should answer the appropriate question no.

There can hardly be any doubt that the studies and research undertaken by the Plaintiffs at the universities were of some benefit to the Plaintiffs as well as to Westinghouse. So, you should carefully consider the words "primary" and "primarily" as used in these instructions.

"Primary" means fundamental, chief, or principal. "Primarily" means fundamental, chiefly, or principally. They mean of first importance, or they mean first in importance.

Was the primary purpose of the studies or research to further the education and training of the Plaintiffs as individuals? Was the primary purpose of the studies and research to further the Plaintiffs' education and training so that they could secure their degrees of Doctors of Philosophy?

Or, were the studies or research primarily for the benefit of Westinghouse? Was the additional education and training the Plaintiffs received and the theses topics and degrees of Doctor of Philosophy to be secured by

[438] them primarily for the benefit of Westinghouse?

The Defendant contends that the amounts or stipends paid to the Plaintiffs during their educational leave are not to be considered scholarships or fellowship grants. The Defendant contends that the Plaintiffs failed

to prove that the stipends they received were scholarships by a fair preponderance of the evidence.

The Defendant wants you to believe from the evidence and the reasonable inferences to be drawn therefrom that the stipends represent compensation for past, present or future employment services performed by Plaintiffs for Westinghouse, or that they represent payments for services performed by Plaintiffs for Westinghouse subject to the direction and supervision of Westinghouse.

Also, the Defendant wants you to believe from the evidence that the studies and research undertaken by the Plaintiffs were primarily for the benefit of Westinghouse.

The Defendant wants you to find the stipends paid to the Plaintiffs are not scholarships excludable from gross income, and therefore the income taxes paid by Plaintiffs on the stipends were legally and correctly assessed. In other words, the Defendant wants you to answer the questions no.

Each Plaintiff has the burden of proving by a fair preponderance of the evidence that his stipend was received by him as a scholarship excludable from gross
[439] income, and therefore the assessment of income taxes on his stipend is illegal and erroneous.

In other words, each Plaintiff has the burden of proving to you by a fair preponderance of the evidence that the primary purpose of his studies and research while on educational leave was to further his education and training and that his studies and research were not primarily for the benefit of Westinghouse.

Also, that the stipend received by him from Westinghouse to enable him to pursue his studies and research did not represent compensation for employment services to Westinghouse, or represent services which were subject to the direction or supervision of Westinghouse.

By a fair preponderance of the evidence, we mean by testimony which appears to you the jury to be more credible and probable—that is, more believable—than the evidence to the contrary.

A fair preponderance of the evidence means the greater weight of the evidence. It is not the greater amount nor the greater number of witnesses. It means that the greater weight, logic and persuasive nature of the believable and

credible evidence leads you to believe that a proposition is true.

By a fair preponderance of the evidence, we mean by such proof as satisfies the conscience and carries
[440] conviction to an intelligent, fair and impartial mind.

When a litigant has proved a fact by a fair preponderance of the evidence, it means that the jury is satisfied that the evidence tending to prove that fact is more probably true than the evidence to the contrary.

If after considering all the testimony and other evidence in the case you are not persuaded by either party, or if the evidence of both sides is of equal weight, then the disputed fact has not been proved by a fair preponderance of the evidence.

In that event, you should answer the questions submitted to you in the negative. In other words, if the Plaintiffs have failed to meet their burden of proof, then you should answer the questions no.

• • •

[441]

• • •

(The jury was withdrawn from the courtroom, and the following occurred out of their hearing.)

• • •

Mr. Larrimer: I would like to take a specific exception to the last comments on the burden of proof, tied in with the charge relating to credibility of witnesses, for the reason that there is no controverted fact in issue, and it is a matter of the jury finding certain facts or not which are material to the decision under the Court's charge.

In other words, I envision that the jury may be
[442] so confused—

The Court: That is very probable.

Mr. Larrimer: That it will ultimately end up to be that because they are confused the Plaintiffs lose.

The Court: That may very well be. The Plaintiffs wanted a jury trial. And, the Plaintiffs have had a jury trial.

I don't know what else I could say. I can see some merit in your objection.

Mr. Larrimer: Well, I—

Mr. Arkin: May I specifically answer that before he goes on?

The Court: Wait a minute. What else do you have?

Mr. Larrimer: Well, Your Honor, my objection is entirely to the fact that Your Honor has told the jury what the regulations are and you have incorporated in your charge both the Government's points or contentions and the Plaintiffs', and I submit it cannot be both. It is either one or the other.

And, I think that that is the confusion that has been created, because we haven't been able to agree on the tests to be applied by the jury.

And, I specifically then except to any charge relating to services subject to the supervision or control of the grantor for the reason that there is no evidence of
[443] services—

The Court: I couldn't see any myself, but they said that there was a package deal here. I am afraid to take it out without his consent. And, he wouldn't consent on Wednesday, so I left it in.

Mr. Larrimer: I make the further exception to the charge which points at one time in the charge to the issue being whether or not the primary purpose of the studies and research was to benefit the Plaintiffs in their individual capacities, or whether it represents compensation for services, past, present or future, or subject to the control and supervision of the grantor. For, I think that it is not necessary to exclude the latter—the compensation for services—in order for it to be considered a scholarship where the man is a candidate for a degree at an educational institution.

And, also for the further reason that there is no evidence that there were services rendered, past, present or future, or subject to the control and supervision of the grantor.

I also except to that portion of the charge which allows the jury to consider who derives the primary benefit from the research and study. There is no evidence that Westinghouse derived any benefit from this.

I specifically take exception to the charge of the Court that the jury may consider in this case the evi-
[444] dence relating to the manner in which the amount of the stipend was determined, the source of the

stipend, the consideration of the Plaintiffs as employees by Westinghouse, the withholding of tax by Westinghouse, or the needs of the Bettis Laboratory for personnel.

The reason I take this exception is I think it is totally irrelevant, and particularly so when the Court did not tell the members of the jury in what manner this could be relevant in arriving at a decision.

That is all.

The Court: As to your first point, you still didn't tell me what you think I ought to have said.

Mr. Larrimer: I don't remember now—oh, that was the burden of proof. Well, I think the burden of proof ties in with the contention—

In other words, I think if Your Honor feels that the Government's contention is right—if that is a contention that is adopted by the Court as the law in this case—then the jury should be told that if they find these facts exist and they are not controverted, then they should find for the Defendant.

The Court: Well, the inferences from the facts are strenuously controverted.

Mr. Larrimer: Well, I don't think—

The Court: Well, all right. I still don't know [445] what you want me to say.

Mr. Larrimer: What I would want you to say, Your Honor, is that the test is whether or not—and the reason I boil it down to this area is that this is the only possible fact which may be in issue—I would ask the Court to charge that the sole test is whether or not the studies and research were primarily for the benefit of the Plaintiffs in their individual capacities.

The Court: The rule doesn't say that. It says if the primary purpose of the studies or research is to further the education and training of the recipients in their individual capacities.

Mr. Larrimer: Yes, sir.

The Court: It doesn't say anything about benefit. But, go ahead.

Mr. Larrimer: Well, I would think that that is the test which Your Honor just stated, the primary purpose of the research and studies. And, whether or not there is a compensatory feature to the stipend is irrelevant.

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[447]

* * *

(The jury retired for deliberation.)

* * *

[449]

* * *

(After due deliberation, the jury returned with answers to the interrogatories in the negative, which verdicts were read by the clerk.)

* * *

(Whereupon the hearing concluded.)

Plaintiff's Exhibit No. 2

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF PENNSYLVANIA

December 4, 1957
(Revised Effective July 21, 1960)

WESTINGHOUSE BETTIS FELLOWSHIP AND DOCTORAL PROGRAMS

Statement of Purpose and General Regulations

I. GENERAL

A. *Purpose*

To provide advanced educational opportunities leading to the Doctor of Philosophy degree for exceptional graduates in engineering and science to aid in meeting the needs of Westinghouse for key professional personnel.

B. *Eligibility*

Participants in those programs are regular Westinghouse Bettis employes with all of those benefits and responsibilities which normally accrue to professional employes of the Westinghouse Bettis Atomic Power Laboratory. In every case, the individual should clearly understand that continuation in the program will depend upon a consistently high level of performance on both his work assignment and his academic program.

(Revised 7/21/60)

Each participant must maintain those contacts with his major advisor, his department head, and other university officials as may be required to make certain that he is pursuing an acceptable program of study in a satisfactory manner.

II. Rules and Regulations

A. *Work-Study Phase—Requirements and Conditions*

1. Throughout this phase of the program, at least once per semester, the participant will have personal interviews with the Administrator of Fellowship and Doctoral Programs, Bettis Education and Training, for the purpose of determining his continued eligibility in terms of his Bettis work assignment and his academic progress.

2. The participant has the responsibility of keeping his supervisor informed about his progress in the program.

3. Requirements to continue on the program:

a. During each fall and winter trimester or fall and spring semester a participant must complete at least six credits (or the equivalent in course units) in courses required in pursuit of the degree. A participant may also continue his academic progress during the spring trimester or the summer session by registering for three credits of required course work. Language courses for the purpose of determining the number of required course credits are excluded.

(Revised 7/21/60)

b. Participating universities set the minimum academic standards required of a candidate for a graduate degree. If a participant fails to meet these minimum standards, his fellowship will be withdrawn.

Apart from academic standards, the privilege of participating in a Bettis Fellowship or Doctoral Program calls for outstanding performance on the part of all participants. If a participant's quality point average falls below 3.25, his eligibility to continue as a Fellowshp participant will be reviewed by the Administrator of the

Fellowship and Doctoral Programs. The quality point average will be found under the following grade system:

A = 4 quality points
B = 3 quality points
C = 2 quality points
D = 1 quality point
F = 0 quality points

(Revised 7/21/60)

If a participant's cumulative quality point average remains below the 3.25 level for the 9 credits following the failure to meet the 3.25 quality point average, his fellowship or doctoral program will be withdrawn.

c. The failure of a required course will be sufficient cause for withdrawal of a participant's fellowship. If the failure is incurred by a participant otherwise in good standing, his fellowship will be suspended until the failed course is retaken and passed with an A or B grade; this honor grade must be earned the next time the course is offered (in any case within two years), and the course failed must be taken at the student's own expense. A participant will be eligible to apply for reimbursement under the Westinghouse Educational Assistance Program for courses taken, other than the failed course, during the period in which his fellowship is suspended.

d. Continued employment and a high level of job performance within the bounds of the work week are requirements for continuation of the program.

(Revised 7/21/60)

e. A participant may interrupt his program of study only in the case of a military leave of absence in accordance with Part II, Section A, Paragraphs 5 and 6.

(Added 7/21/60)

4. It is the responsibility of a participant to ascertain his eligibility to continue on the program. If he should register for courses while ineligible, he will not be reimbursed for any tuition, texts, or fees associated with these courses.

5. A participant going on military leave of absence is required to notify the Administrator of Fellowship and Doctoral Programs, Bettis Education and Training, at least ten days prior to beginning of the leave. If it is anticipated that a military leave of absence is to begin during an academic semester, the participant will not register for courses during that semester.

6. A participant on military leave of absence must apply to the Administrator of Fellowship and Doctoral Programs, Bettis Education and Training, for reinstatement of his fellowship at least four months prior to his separation from the armed services. If the participant was in good standing at the time of leaving for military service, the request for reinstatement may be granted provided the program still exists and funds are available.

7. A participant is expected to complete all courses for which he registers. When a participant finds it necessary to drop a course, he is expected to do so within that period in which the university reimburses the full tuition.

B. *Work-Study Phase—Remuneration and Reimbursement*

1. Subject to conditions and limitations set forth below in Section II, Part B, Paragraph 2, participants in these programs will be employed by the Bettis Atomic Power Laboratory on a 40 hours-per-week basis with release time of up to eight hours per week to attend required graduate courses.

(Revised 7/21/60)

2. When a participant's anticipated rate of release time exceeds 156 hours distributed over the fiscal year, those hours in excess of that rate will either be uncompensated or made up on a mutually agreed upon work schedule.

a. Each participant must submit a specific written request for release time to the Administrator of Fellowship and Doctoral Programs, Bettis Education and Training, at the time of registration. This request will be reviewed and the approved schedule will be forwarded to the participant's supervisor for his concurrence and information.

(Added 7/21/60)

b. When each semester or trimester release time schedule is approved, the Administrator of Fellowship and Doctoral Programs will inform the participant's supervisor of the number of release hours, if any, that exceed the maximum rate of 156 release hours per fiscal year. It is the responsibility of the participant's supervisor to determine whether the participant will make up those release hours in excess of 156 or whether the participant's salary will be reduced accordingly. The supervisor will take the appropriate administrative action and inform the Administrator of Fellowship and Doctoral Programs of the agreed upon work schedule.

3. When a participant is not attending required courses he is to assume the regular 40-hour work week schedule.

(Revised 7/21/60)

4. Participants may not be scheduled or compensated for overtime work while enrolled for course or thesis work during the work-study phase of the Fellowship and Doctorial Programs.

5. In addition to the specified salary and tuition remuneration, the Westinghouse Electric Corporation will reimburse Fellowship and Doctoral Program participants for fees and textbooks required of all students pursuing a program for an approved graduate degree. Participants will not be reimbursed for fines, deposits, and reference books or special fees.

The reimburseable fees for the MS degree are:

a. Laboratory fees

b. Thesis binding fees

c. Graduation fee

d. Rental fee for cap, gown, and hood

Refundable deposits such as the deposit for cap, gown, and hood will not be reimbursed.

Tuition for only six thesis credits will be reimbursed at the MS level.

6. Course credits or terms of residence beyond those normally required for the satisfaction of the requirements

for the Ph.D. degree will be reimbursed only upon the written recommendation of the participant's major advisor and with the concurrence of the Administrator of Fellowship and Doctoral Programs, Bettis Education and Training. In any case, reimbursement will be made only for courses taken for credit.

C. *Educational Leave Phase—Application and Approval*

1. The conditions of eligibility for continuing on the work-study phase of the Bettis Fellowship and Doctoral Programs are set forth in definite terms. However, successful candidates for the Educational Leave Phase of the Programs are selected from among applicants who have satisfactorily completed the work-study phase. Accordingly, if the number of candidates exceeds that for which financial support is available, a Fellowship Review Board will determine those who are to go on Educational Leave.

(Added 7/21/60)

2. Educational Leave will be granted for the specific purpose of completing the doctoral dissertation.

(Revised 7/21/60)

3. Each participant is urged to explore fully the possibility of conducting his doctoral dissertation in an area of technical interest to Bettis. In making his search for a desirable thesis topic, a participant is expected to consult with Bettis Laboratory technical supervisors for suggestions.

(Added 7/21/60)

4. To insure adequate time for planning and for gathering of the information required for obtaining approval of each participant's educational leave, the participant is responsible for notifying the Administrator of Fellowship and Doctoral Programs, Bettis Education and Training, of the proposed starting date of the participant's leave at least six months prior to that date.

(Revised 7/21/60)

5. Candidates, when qualified and ready for leave will make formal application for leave to Education and Train-

ing. The Educational leave Application forms, available in the office of the Administrator of Fellowship and Doctoral Programs, Bettis Education and Training, must be completed and submitted to that office at least three months prior to the proposed starting date.

(Revised 7/21/60)

6. To insure maximum benefits from his period of educational leave the participant should be prepared to show that he has:

a. Successfully completed all course requirements for the doctoral degree as specified by his department.

b. Successfully completed the comprehensive examinations required by his department and satisfied all requirements for admission to candidacy for the doctoral degree.

c. Selected a thesis topic with the concurrence of his major advisor and department head.

d. Available to him all facilities and equipment reasonably anticipated as necessary for the completion of the thesis.

7. A Fellowship Review Board consisting of the Executive Assistant to the General Manager, the Manager, Education and Training, and one or more members of senior Laboratory management will review the participant's application for Educational Leave taking into consideration the candidate's record, the needs of the Laboratory, and funds available.

(Added 7/21/60)

The Board may consult with technical supervisors and management and may interview the applicant as required to reach their decision which may be one of the following:

a. An educational leave may be approved, subject to A.E.C. approval.

b. A leave may be approved, subject to A.E.C. approval, but deferred until the next fiscal year.

c. The educational leave may be disapproved.

D. *Educational Leave Phase—Reimbursement and Conditions*

1. During the period of educational leave a participant in a Westinghouse Fellowship or Doctoral Program will receive an educational stipend. The stipend will be determined on the following basis:

a. A stipend of 70 per cent of the base salary and adders of a single participant with a maximum of $490 per month gross.

b. A stipend of 80 per cent of the base salary and adders of a married participant with a maximum of $560 per month gross.

(Revised 7/21/60)

c. A stipend of 85 per cent of the base salary and adders of a married participant with one child with a maximum of $595 per month gross.

d. A stipend of 90 per cent of the base salary and adders of a married participant with two or more children with a maximum of $630 per month gross.

2. For the purpose of the above calculations the base salary and marital status will be that of the participant at the time his leave is initiated. However, if a participant's status changes while on educational leave, he should apply to the Administrator of Fellowship and Doctoral Programs, Bettis Education and Training, for a change in stipend in keeping with his change in status. Salary changes accruing to all Westinghouse employees such as general wage increases will be reflected in a participant's stipend up to the maximum amount provided in Part II, Section D, Paragraph 1.

(Revised 7/21/60)

3. While on educational leave a participant will be reimbursed for tuition and fees normally required by the participant's school of candidates for a given degree. The reimburseable fees are:

(Revised 7/21/60)

a. Laboratory fees

b. Cost of publication of doctoral dissertation and abstract

c. Dissertation binding fees

d. Graduation fee

e. Rental fee for cap, gown, and hood

Cost of translations and textbooks and the typing and reproduction of the thesis are not reimburseable. Refundable deposits such as the deposit for cap, gown, and hood will also not be reimbursed.

(Revised 7/21/60)

4. Tuition of up to two and one-half terms of residence, if required, will be reimbursed after a participant has initiated educational leave at the University of Pittsburgh; tuition of up to two semesters on a full-time basis and 12 additional units, if required, will be reimbursed after a participant has initiated educational leave at the Carnegie Institute of Technology.

(Added 7/21/60)

5. Educational Leave will be granted for an academic year of nine months; however, upon request the leave period may be granted for a calendar year of twelve months with the stipulation that the stipend that would normally be received during a nine-month leave period be spread over the twelve month period. A participant initially selecting a nine month leave period may request a 3 month extension. Westinghouse may finance this extension by extending his stipend for 3 months on a loan basis at no interest. A participant utilizing the loan service must repay it, upon his return from leave, by authorizing payroll deduction at a minimum rate of $100 per month. When circumstances warrant, the Manager, Education and Training, may permit a participant who does not complete his dissertation within the formal leave period to continue work on his dissertation on a release-time basis for one additional trimester or semester.

(Added 7/21/60)

6. When a participant's major advisor recommends that an additional period beyond 12 months of full-time leave is necessary, a review will be made by the Fellowship Review Board, and a leave extension on a to-be-determined loan

or part-time work basis may be granted. In no case, however, may the total of all loans exceed the equivalent of three months' leave stipend computed at the monthly rate the participant would receive on a nine-month leave basis.

(Added 7/21/60)

7. Each participant initiating educational leave or an extension of leave on or after July 1, 1960 will sign an employment agreement with Westinghouse, at the time he applies for his educational leave, or extension of leave. Each participant will agree that after the end of his educational leave he will assume such duties commensurate with his education and experience as may be assigned to him by Westinghouse, and will thereafter continue in the employ of Westinghouse for at least two (2) calendar years from the date he assumes those duties at a rate of salary commensurate with the duties assigned.

(Revised 7/21/60)

E. *General Conditions*

1. All participants will be subject to Atomic Energy Commission, Navy or Department of Defense regulations or requirements with respect to Fellowship and Doctoral Programs which may come into effect.

2. The support of the Bettis Fellowship and Doctoral Programs must be on a year-to-year basis. While Westinghouse has every intention of continuing its support, circumstances beyond its control may alter the conditions of support in future years.

(Added 7/21/60)

3. The Manager, Bettis Education and Training, has the right to change with notice, or to waive any of these rules and regulations under circumstances which warrant such action.

Defendant's Exhibit No. I

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF PENNSYLVANIA

EMPLOYMENT AGREEMENT

Agreement made this 30th day of October 1961, between Westinghouse Electric Corporation (hereinafter referred to as Westinghouse) and Mr. Martin L. Pomerantz (hereinafter referred to as Mr. Pomerantz).

It is agreed:

1. Westinghouse will reimburse Mr. Pomerantz for tuition and required fees while in attendance at University of Pittsburgh for the period from November 1, 1961 to July 31, 1962 under Westinghouse Bettis Atomic Power Laboratory Fellowship Program in Mechanical Engineering.

2. Westinghouse will pay Mr. Pomerantz the sum of $630.00 per month until the completion of the educational leave or until this Agreement is terminated, whichever occurs first.

3. After the end of the educational leave Mr. Pomerantz will assume such duties commensurate with his education and experience as may be assigned to him by Westinghouse, and will thereafter continue in the employ of Westinghouse for at least two (2) calendar years from the date he assumes those duties, at a rate of salary commensurate with the duties assigned.

This Agreement may be terminated by Westinghouse at any time by giving notice to Mr. Pomerantz of such termination. In the event of termination, for any reason, Westinghouse will have no liability hereunder to Mr. Pomerantz because of or after such termination.

IN WITNESS WHEREOF, the parties have hereunto set their hands and seals on the day first above written.

W. A. QUINN
Witness

ATTEST: ! ! ! ! !

MARTIN L. POMERANTZ

WESTINGHOUSE ELECTRIC CORPORATION

By: CLYDE E. VOGELEY

Defendant's Exhibit No. 3

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF PENNSYLVANIA

EMPLOYMENT AGREEMENT

Agreement made this 16th day of September 1960, between Westinghouse Electric Corporation (hereinafter referred to as Westinghouse) and Mr. R. E. Johnson (hereinafter referred to as Mr. Johnson).

It is agreed:

1. Westinghouse will reimburse Mr. Johnson for tuition and required fees while in attendance at Carnegie Institute of Technology for the period from October 1, 1960 to June 30, 1961 under Westinghouse Bettis Atomic Power Laboratory Doctoral Program in Metallurgy.

2. Westinghouse will pay Mr. Johnson the sum of $630 per month until the completion of the educational leave or until this Agreement is terminated, whichever occurs first.

3. After the end of the educational leave Mr. Johnson will assume such duties commensurate with his education and experience as may be assigned to him by Westinghouse, and will thereafter continue in the employ of Westinghouse for at least two (2) calendar

years from the date he assumes those duties, at a rate of salary commensurate with the duties assigned.

This Agreement may be terminated by Westinghouse at any time by giving notice to Mr. Johnson of such termination. In the event of termination, for any reason, Westinghouse will have no liability hereunder to Mr. Johnson because of or after such termination.

IN WITNESS WHEREOF, the parties have hereunto set their hands and seals on the day first above written.

W. A. QUINN
Witness

ATTEST: J. EVANS

RICHARD EDWIN JOHNSON

WESTINGHOUSE ELECTRIC CORPORATION

By: JOHN R. VAN HORN

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF PENNSYLVANIA

CIVIL ACTION No. 65-1033

RICHARD E. JOHNSON and BEVERLY P. JOHNSON, his wife, and MARTIN L. POMERANTZ and PHYLLIS L. POMERANTZ, his wife, and RICHARD A. WOLFE and ANNE F. WOLFE, his wife, *Plaintiffs*

v.

JOHN H. BINGLER, District Director of Internal Revenue, *Defendant*

Judgment

This case was called in open court on November 21, 1966 and there appeared James Larrimer, Esquire, for the plaintiffs and Michael B. Arkin, Esquire, for the defendant.

All parties announced ready and a jury was impaneled and sworn. Counsel for the parties stated the case, evi-

dence was introduced by the parties and the case was argued by counsel for the parties.

The Court instructed the jury as to the law; the jury retired to consider the evidence and returned with answers to special interrogatories as follows:

1. Were the amounts received by Richard E. Johnson from Westinghouse a scholarship at an educational institution excludable from his gross income?

ANSWER "YES" OR "NO" "No"

2. Were the amounts received by Martin L. Pomerantz from Westinghouse a scholarship at an educational institution excludable from his gross income?

ANSWER "YES" OR "NO" "No"

3. Were the amounts received by Richard A. Wolfe from Westinghouse a scholarship at an educational institution excludable from his gross income?

ANSWER "YES" OR "NO" "No"

In accordance therewith, it is hereby:

ORDERED, ADJUDGED and DECREED that plaintiffs' complaint be and the same is hereby dismissed with prejudice and judgment is hereby entered in favor of the defendant, together with costs to be awarded to the defendant.

/s/ RABE F. MARSH

Honorable Rabe F. Marsh
United States District Judge for the Western District of Pennsylvania

December 2nd, 1966

Certified from the record, Date 12-6-66, JAMES H. WALLACE, JR., Clerk.

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF PENNSYLVANIA

[Title omitted in Printing]

Motion for New Trial

AND NOW come the plaintiffs, by their counsel, and request the Court to set aside the verdict in favor of the defendant and the judgment entered thereon and to award a new trial for the following reasons:

1. The verdict is against the law.

2. The verdict is against the evidence.

3. The verdict is against the law and the evidence and the weight of the evidence.

4. Prejudicial error was committed by the admission into evidence of testimony relating to the benefit to be derived by Westinghouse and the Atomic Energy Commission from the overall scholarship program involved in the action, independent of the benefit which may have been derived, if any, from the specific research conducted by the individual plaintiffs.

5. Prejudicial error was committed by the admission into evidence of the accounting procedures utilized by Westinghouse in recording the stipends received by the plaintiffs.

6. Prejudicial error was committed by the admission into evidence of the fact that tax was withheld from the stipend.

7. Prejudicial error was commited by the admission into evidence of the testimony relating to the purpose of Westinghouse in initiating the scholarship program involved.

8. Prejudicial error was committed by the admission into evidence of testimony relating to the contractual relationship between Westinghouse Electric Corporation and the Atomic Energy Commission.

9. Prejudicial error was committed by the admission into evidence of the Westinghouse employee benefit plans, pension plan, profit-sharing, etc.

10. A new trial should be granted because the instructions of the Court to the jury were inadequate in the following respects:

A. The charge as a whole was inadequate since it did not clearly state to the jury what factual finding or findings were important in arriving at the verdict.

B. The charge of the Court was inadequate in that it did not state precisely the legal principles involved but rather adopted the contentions of both the plaintiffs and the defendant and told the jury to make its selection.

C. The charge of the Court was inadequate in that it directed the jury to consider the evidence relating to the basis for fixing the amount of the stipend, the source of the stipend, the consideration of the plaintiffs by Westinghouse as employees, the fact that withholding tax was withheld and the needs and requirements of Bettis Laboratory for personnel without further instructing the jury as to the relevancy of such evidence.

D. The charge of the Court was erroneous in that it charged on the matter of service rendered to Westinghouse or the Atomic Energy Commission by the plaintiffs during the educational leave period when there was no evidence that services were rendered.

E. The charge was erroneous in that it instructed the jury on the primary benefit derived by Westinghouse from the research conducted by the plaintiffs when there was no evidence that Westinghouse derived any benefit from the research.

F. The charge was erroneous in that it instructed the jury on compensation for past, present or future services when there was no evidence of such past, present or future services.

G. The charge was erroneous in that it instructed the jury in effect that the stipend could not be considered a scholarship if it was in effect compensatory to the plaintiffs.

H. The charge was erroneous in that it charged on services being subject to the supervision of the grantor

when there was no evidence that there were such services or that such services, if any, were subject to any supervision or control by the grantor.

11. The charge of the Court was inadequate and prejudicial to the plaintiff because of the fact that it was confusing to the jury, did not clearly state to the jury the legal principles involved in view of the fact that the basic facts were undenied, and in view of the fact that the closing statements of the charge reminded the jury of the burden of proof being on the plaintiffs.

12. The Court erred in not affirming the plaintiffs' points for charge, Nos. 7, 8, 9, 10, 11, 12, 13, 15, 16, 17, 18, 19 and 20.

13. The error was committed in submitting the Interrogatories to the jury which suggested that there may be a scholarship at an educational institution which was not excludable from gross income.

14. The plaintiffs reserve the right to assign such further reasons for a new trial as may become apparent after the transcript of testimony becomes available for inspection.

DOUGHERTY, LARRIMER & LEE

By /s/ JAMES C. LARRIMER
Attorneys for Plaintiffs

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF PENNSYLVANIA

Civil Action No. 65-1033

RICHARD E. JOHNSON and BEVERLY P. JOHNSON, his wife, and MARTIN L. POMERANTZ and PHYLLIS L. POMERANTZ, his wife, and RICHARD A. WOLFE and ANNE F. WOLFE, his wife, *Plaintiffs*

vs.

JOHN H. BINGLER, District Director of Internal Revenue, *Defendant*

Opinion and Order

MARSH, *District Judge.*

In this action plaintiffs sue for the refund of income taxes alleged to have been erroneously assessed and collected from the plaintiffs for certain taxable years. Pretrial Stipulation, I.[1] Jurisdiction arises pursuant to Title 28 U.S.C.A. § 1340. The male plaintiffs (hereinafter plaintiffs) were employees of Westinghouse Electric Corporation (Westinghouse); each was granted educational leave to obtain a Ph.D. degree in mechanical engineering (Johnson) or metallurgical engineering (Pomerantz and Wolfe) at Carnegie Institute of Technology (Johnson and Wolfe) or the University of Pittsburgh (Pomerantz) pursuant to the Westinghouse Bettis Fellowship and Doctoral Program; each obtained a Ph.D degree and thereafter, in compliance with a written employment agreement with Westinghouse (Johnson and Pomerantz) or oral understanding (Wolfe), each continued in the employ of Westinghouse for at least the required length of time. Pretrial Stipulation, III, IV.

1

"Plaintiff	Amount	Year
Richard E. Johnson and	$395.00	1960
Beverly P. Johnson	599.82	1961
Martin L. Pomerantz and	276.68	1961
Phyllis L. Pomerantz	312.10	1962
Richard A. Wolfe and	985.31	1960
Anne F. Wolfe	362.24	1961"

The plaintiff wives were named only because there were joint income tax returns filed for the years involved. Pretrial Stipulation, III.

During plaintiffs' educational leaves Westinghouse paid their tuition at the educational institution and stipends based on a percentage of their base salaries plus family allowance. Westinghouse withheld and paid income tax on the stipends which are the amounts plaintiffs seek to have refunded.

A jury trial was held pursuant to the demand of the plaintiffs. The jury was asked with respect to each plaintiff:

> "Were the amounts received by [name of plaintiff] from Westinghouse a scholarship at an educational institution excludable from his gross income?"

Each question was answered in the negative. Plaintiffs ask for a new trial alleging errors in the admission of evidence and in the instructions. In our opinion a new trial should be denied.

Fellowships and scholarships are excluded from a taxpayer's gross income. Title 26 U.S.C.A., §§ 61(a), 117. The pertinent regulations provide:

> "§ 1.117-4 *Items Not Considered as Scholarships or Fellowship Grants.* The following payments or allowances shall not be considered to be amounts received as a scholarship or a fellowship grant for the purpose of section 117:
>
> "• • •
>
> "(c) *Amounts paid as compensation for services or primarily for the benefit of the grantor.*
>
> "(1) Except as provided in paragraph (a) of § 1.117-2, any amount paid or allowed to, or on behalf of, an individual to enable him to pursue studies or research, if such amount represents either compensation for past, present, or future employment services or represents payment for services which are subject to the direction or supervision of the grantor.
>
> "(2) Any amount paid or allowed to, or on behalf of, an individual to enable him to pursue studies or research primarily for the benefit of the grantor.
>
> "However, amounts paid or allowed to, or on behalf of, an individual to enable him to pursue studies or

> research are considered to be amounts received as a scholarship or fellowship grant for the purpose of section 117 if the primary purpose of the studies or research is to further the education and training of the recipient in his individual capacity and the amount provided by the grantor for such purpose does not represent compensation or payment for the services described in subparagraph (1) of this paragraph. Neither the fact that the recipient is required to furnish reports of his progress to the grantor, nor the fact that the results of his studies or research may be of some incidental benefit to the grantor shall, of itself, be considered to destroy the essential character of such amount as a scholarship or fellowship grant."

We think that the plaintiffs had the burden of proof. *Niles Bement Pond Co.* v. *United States*, 281 U.S. 357; *United States* v. *Rindskopf*, 105 U.S. 418; *United States* v. *Lease*, 346 F. 2d 696 (2d Cir.). Although for the most part the facts were undisputed, the reasonable inferences to be drawn therefrom were hotly contested. Those inferences and the ultimate fact embodied in the verdicts were for the determination of the jury. The items of evidence which plaintiffs contend were erroneously admitted, in our opinion were relevant to the underlying issues of fact imposed upon the fact finder by the quoted regulation. The instructions to which plaintiffs excepted were capably argued to the court at length by the expert counsel prior to their arguments to the jury and represent the distillation of counsels' views and the opinion of the court as to the law of the case. See: *Ussery* v. *United States*, 296 F. 2d 582 (5th Cir. 1961); *C.I.R.* v. *Ide*, 335 F. 2d 852 (3d Cir. 1964); *Stewart* v. *United States*, 363 F. 2d 355 (6th Cir. 1966); *Wells* v. *Commissioner*, 40 T.C. 40 (1963); *Woddail* v. *C.I.R.*, 321 F. 2d 721 (10th Cir. 1963); *Reiffen* v. *United States*, Court of Claims, filed February 2, 1967. The jury's attention was directed to the undisputed and disputed facts as they related to the law and as they applied to the theories advanced by each side. To the jury were submitted the determination of the verdicts and the all important inferences which could be reasonably drawn from the evidence. Those inferences, pro and con, were completely and fully argued to the jury by counsel. If, as plaintiffs so vigorously contend in their

brief, the evidence requires the entry of judgment notwithstanding the verdicts, they will have to persuade the reviewing court to make that decision, for although considerable merit is recognized in their arguments on the law, this court is not persuaded that the case as brought and tried did not present issues of fact for the jury.

An appropriate order will be entered.

Order of Court

AND NOW, to-wit, this 3rd day of July, 1967, after argument and upon due consideration of the briefs submitted, IT IS ORDERED, ADJUDGED AND DECREED that the plaintiffs' Motion for a New Trial be and the same hereby is denied.

(signed) RABE F. MARSH
United States District Judge

cc:

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UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

Nos. 16826, 16827 & 16828

RICHARD E. JOHNSON and BEVERLY P. JOHNSON, his wife, and MARTIN L. POMERANTZ and PHYLLIS L. POMERANTZ, his wife, and RICHARD A. WOLFE and ANNE F. WOLFE, his wife

v.

JOHN H. BINGLER, District Director of Internal Revenue
RICHARD E. JOHNSON and BEVERLY P. JOHNSON, his wife,
Appellants in No. 16826

MARTIN L. POMERANTZ and PHYLLIS L. POMERANTZ, his wife,
Appellants in No. 16827

RICHARD A. WOLFE and ANNE F. WOLFE, his wife,
Appellants in No. 16828

APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF PENNSYLVANIA

Argued January 18, 1968

Before HASTIE *Chief Judge*, GANEY, *Circuit Judge*, and WEINER, *District Judge*

Opinion of the Court

(Filed June 5, 1968)

By WEINER, *District Judge*

Before us on this appeal are three taxpayers[1] who, while employees of the Westinghouse Electric Corporation, were participants in the Westinghouse Bettis Fellowship and Doctoral Program through which each received a

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[1] Appellants' wives are joined as nominal plaintiff-appellants by virtue of the joint income tax returns filed by them with their husbands for the years involved.

stipendiary grant and leave of absence from his employer in order to research, write and defend his Ph.D. thesis in engineering at either the University of Pittsburgh or Carnegie Institute of Technology (now Carnegie-Mellon University).

There was testimony below that the Bettis Atomic Power Laboratory, at which each taxpayer was employed before and after his academic leave of absence, is owned by the United States Government and is operated by Westinghouse under a "cost-plus" type of contract with the Atomic Energy Commission. Appellants' theses related to the work program of the Laboratory in the field of nuclear engineering.

Income tax was withheld from the monthly allowances received by each of the three appellants; each filed a claim for refund of this tax on the grounds that the grant was excludable from his gross income as a scholarship under Int. Rev. Code of 1954, § 117. These claims were rejected by the Internal Revenue Service, and again by a jury in the trial below.

The correctness of this determination is the subject of this appeal.

The crucial terms "scholarship" and "fellowship grant" appear in the revelant § 117 without any definition whatsoever.[2] In the absence of any guidance as to the content of these statutory concepts embodied in the Code itself, we agree with the Tax Court that

> "a proper reading of the statute requires that before the exclusion comes into play there must be a determination that the payment sought to be excluded has the normal characteristics associated with the term 'scholarship.'"

---

[2] In pertinent part, § 117(a)(1) provides as follows:

"(a) General rule.—In the case of an individual, gross income does not include—

(1) any amount received—

(A) as a scholarship at an educational institution (as defined in section 151(e)(4)), or

(B) as a fellowship grant . . ."

26 U.S.C. § 117(a)(1).

Elmer L. Reese, Jr., 45 T.C. 407, 413 (1966), *aff'd per curiam*, 373 F.2d 742 (4th Cir. 1967). Without attempting a comprehensive definition, we can simply mention some of the more salient "normal characteristics" of such scholarships or fellowship grants that are exemplified in the situation before us.

Appellants' stipends were awarded as subsidies to full-time students, in an amount bearing an appropriate relation to each recipient's needs. Their continuance was contingent upon the participant's maintenance of the academic standards required of a candidate for a graduate degree by the university which each appellant attended. While receiving these grants, appellants were on an academic leave of absence from their employment for the specific purpose of completing their doctoral dissertations. These are the most important positive characteristics which appellants' grants shared with scholarships generically. We turn now to the Code and the legislative history for an understanding of the distinctions with which Congress intentionally colored the kind of grant it wished excluded from gross income for internal revenue purposes.

Most notable in the legislative tax treatment of scholarships is that the Congress in 1954 was painting with a broad brush. Grants which properly qualify as scholarships are excluded from taxation in very unqualified terms by § 117(a). In the case of candidates for a degree, such as appellants before us, this exclusion is explicitly limited in the statute only as not applying

> "to that portion of any amount received which represents payment for teaching, research, or other services in the nature of part-time employment, required as a condition to receiving the scholarship or fellowship grant."

Int. Rev. Code of 1954, § 117(b)(1). The statute as it applies to degree candidates provides no ceiling for the amount that the candidate may exclude from his gross income, as long as it otherwise properly qualifies for scholarship tax treatment. This is in sharp contradistinction to the limit of $300 a month for a maximum of 36 months to which those not candidates for a degree are held. *Compare* § 117(b)(1) *with* § 117(b)(2)(B).

The legislative history also evinces unmistakably the intent of Congress to exclude from tax treatment qualifying scholarships without regard to whether they are to be considered "as income or as gifts," H.R. Rep. No. 1337, 83d Cong., 2d Sess. 15 (1954), as had been the test hitherto applied under the then "existing confusion," *id.*, for which the 1954 change was an attempted remedy. The Senate Report, furthermore, carefully sets out the sequence of the thinking that went into § 117:

> "The section first states the general rule that amounts received as scholarships or as fellowship grants are excludible from gross income and then prescribes specific rules for limiting the amounts which may be excluded."

S. Rep. No. 1622, 83d Cong., 2d Sess. 17 (1954).

In light of the statutory language and the reports of the Congressional committees which drafted it, the dominant legislative intent evident in the scheme of § 117 is that of encouraging financial aid to students at accredited schools, and especially to candidates for degrees, through the device of limited tax relief. The further attention given by both the statute and the legislative history[3] toward limiting the exclusion only for those *not* candidates for a degree would strengthen the inference, by the canon of statutory construction that *expressio unius est exclusio alterius*, that Congress intentionally included the sole restrictions it wished to place on the excludability of scholar-

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[3] H.R. Rep. No. 1337, *supra* at 17 expressed concern, in the case of non-degree candidates, lest the exclusion extent to any annual grant which, together with "any compensation received from the recipient's previous employer," exceeded 75% "of the recipient's salary in the year preceding the grant." In taxing any amount above this limit, the House committee declared: "This will tax those grants which are in effect merely payments of a salary during a period while the recipient is on leave from his regular job." *Id.* For this percentage exclusion the Senate committee "substituted for the 75 percent rule an exclusion of $300 per month of grants paid to individuals who are not candidates for degrees." S. Rep. No. 1622, *supra* at 18. Both committees evidently foresaw the instant problem and legislated with respect to the type of student and the amount of stipend they wished to subject to a limitation on excludability.

ship stipends for degree candidates in the language of § 117(b)(1) itself.

To the sole qualification of § 117(b)(1), then, that degree candidates cannot exclude as tax-exempt scholarships any payment for services required as a condition of the grant, the Treasury Regulations purport to add two others. These would subject to taxation, in pertinent part, any stipend for studies or research which (1) "represents either compensation for past, present, or future employment services"; or which (2) subsidizes studies or research "primarily for the benefit of the grantor." Treas. Reg. 1.117-4(c)(1)-(2) (1956).

In light of the aim explicit in the legislative history of doing away with the touchstone of compensation versus gift, we cannot say, as one court has, that "indicia of compensation" such as are suggested by the regulation are legitimate criteria for testing the excludability of an alleged scholarship, *cf. Stewart* v. *United States,* 363 F.2d 355, 357 (6th Cir. 1966). Nor can we even approve the disqualification added by Treas. Reg. § 1.117-4(c)(1) (1956) of amounts which represent "compensation for past, present, or future employment services," without more. *Contra, Ussery* v. *United States,* 296 F.2d 582, 586-87 (5th Cir. 1961). This ruling seems merely an attempt to write into the regulations a concept which was considered and intentionally rejected by the Congress which enacted the Code.

To summarize: under a fair reading of the Internal Revenue Code of 1954, § 117, in the light of the Congressional committee reports which point up the thinking of the 1954 Congress, we believe that any reasonable stipend which comes within the common understanding of what constitutes a scholarship, is paid to finance the schooling of a degree candidate, and does not fall within the limitation of § 117(b)(1) is excluded from gross income. To illustrate the application of this general outline, we shall take up the Government's arguments in the discussion remaining.

The first element in the Westinghouse Fellowship Program that appears to trouble the Internal Revenue Service is the fact that each grant for those recipients on educational leave was based on a percentage of the

grantee's "base salary".[4] The basis on which each Westinghouse Fellowship grant was calculated was, however, not without some logic other than as what might arguably be a disguised salary payment. Scholarships are characteristically based at least partly on need, and the Westinghouse grants were calculated, perhaps generously, to give each recipient a living allowance based upon the size of his family and the standard of living to which his previous salary had accustomed him, without a sudden substantial cut in revenue. Monthly maxima were set; these ceilings do not appear to us to have been excessive or unreasonable —the one limitation most probably implicit in the otherwise unrestricted excludability of scholarships for degree candidates in § 117.

The concept and content of "scholarship" are developing ones. Fundamental in the exclusion afforded such stipends by § 117 is its encouragement toward graduate study. Without an arrangment of subsidies on a sliding scale based on prior income, employees such as appellants here would probably be hard pressed to leave work for a year to return to school to earn an advanced degree. We think the purpose of the instant fellowship program entirely consistent as concerns appellant degree candidates with the scheme of the exclusion afforded scholarships by the Internal Revenue Code of 1954, § 117. There is, moreover, as we have noted above, no ceiling to this exclusion in the statute.

Although the Senate report on § 117 did not discuss the problem of salary payments disguised as educational stipends for degree candidates, it did display concern for this problem with regard to postdoctoral students. In this connection, it notes: "Such grants may be in effect a continuing salary payment while the recipient is on leave from his regular job," S. Rep. No. 1622, *supra* at 18. The preventive response of Congress, however, was restricted to the $300 monthly limit of § 117(b)(2)(B) for nondegree candidates.

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[4] Depending on the family status of the recipient, a Westinghouse Fellow received a stipend of 70% "of the base salary" plus "adders" up to a monthly maximum of $490 if single; 80% plus adders up to $560 monthly if married; 85% plus adders up to $595 monthly if married with one child; and 90% plus adders up to $630 if married with two or more children.

Hence the Westinghouse grants, even based as they were partly on a percentage of each recipient's prior earnings and partly on family size and need, do not seem to us for this reason to disqualify for exclusion either under the statutory language or because of any alleged failure to meet what we consider to be "the normal characteristics associated with the term 'scholarship'."

The second reason advanced by the Government for disqualifying these grants from nontaxable scholarship treatment is that the grantor, Westinghouse, in its own bookkeeping did not denominate them as such: it carried them, rather, as "indirect labor, or overhead." Deductions from the stipend checks, moreover, were regularly made for income tax and social security payments. An evident discrepancy exists between the characterization of these grants both by appellants and by the Fellowship prospectus as "stipends", on the one hand, and by the custodian of the payroll records at the Westinghouse Bettis Atomic Power Laboratory as "indirect labor", on the other.

The answer to this contention by the Government that the grantor's treatment controls, however, has already been given by this circuit in a similar case, where we recently had occasion to

> "observe and emphasize that under this regulation [§ 1.117-4(c)(2) (1956)] the determinative consideration is not the primary purpose of the grantor in subsidizing the student, but rather the primary purpose of and the primary benefit from the subsidized study."

Commissioner v. *Ide,* 335 F.2d 852, 855 (3d Cir. 1964) (Hastie, J.). Although the court in *Ide* was considering more particularly the taxability of the grants there in question on the grounds that the work done by the grantees was "primarily for the benefit of the grantor," in the words of Treas. Reg. § 1.117-4(c)(2) (1956); nonetheless we believe this observation equally valid as a caution against grafting an additional subjective test based on the grantor's intention onto the existing statutory language which was intended to obviate this inquiry. *Accord, Chandler P. Bhalla,* 35 T.C. 13, 17 (1960) (by implication), *acquiesced in,* 1965-1 Cum. Bull. 4.

The third element of this program to which the Internal Revenue Service objects is the commitment required by the

Westinghouse Bettis Fellowship and Doctoral Programs of each participating fellow:

> "that after the end of his educational leave he will assume such duties commensurate with his education and experience as may be assigned to him by Westinghouse, and will thereafter continue in the employ of Westinghouse for at least two (2) calndar years at a rate of salary commensurate with the duties assigned."

We do not agree with the Government that this commitment, in this case, is sufficient evidence that these stipends were of an essentially "compensatory nature". Compensation for the future "duties" of each grantee is to be at a "commensurate" salary, presumably without adjustment downwards to take account of the instant grant.

Assuming the above clause to be unenforceable by specific performance, we think it nonetheless apparent that contingent liability in damages for the breach of such a clause might be of substantial value in an appropriate factual situation. A significant commitment by the student in return for a grant would, of course, place that grant outside the category "scholarship", at least to the extent of the value of that commitment. For if the grantee had to barter for his stipend, giving full value for it, this arrangement would hardly serve the primary purpose of the § 117 exclusion: to encourage financial aid to education through tax relief.

In the instant situation, however, appellants' promise to return to employment with Westinghouse at an appropriate salary would subject them to no financial sacrifice. They are to be paid in accordance with their enhanced enducational qualifications. Since a salary commensurate to their new duties is already inducement for them to return to their employer-grantor, appellants' additional paper commitment seems of negligible value in this case.

We of course express no opinion as to cases where the quid pro quo given by the grantee for his grant is of measurable monetary value.

Viewed in a light most adverse to appellants, their situation is still akin to that in *Aileene Evans*, 34 T.C. 720 (1960), *acquiesced in*, 1965-1 Cum. Bull. 4. There the Tax Court held petitioner's stipend excludable from her gross income under § 117, even though she was obligated either

to work for her grantor after her studies or to refund the sums advanced. Although petitioner in *Evans* was not an employee of the grantor at the time she received her stipend, we do not deem this distinction material to the hypothetical question of compensation for future employment services.[5]

The last argument advanced by the Government is that appellant's studies were not primarily for the purpose of educating and training each recipient in his individual capacity, but rather in his capacity as an employee of the grantor. The grants, the Government argues, would hence be proscribed by Treas. Reg. § 1.117-4(c)(2) (1956).

To decide this issue, we do not have to consider the validity of this regulation in the light of the statutory language and legislative history of § 117. For the Government's argument is one step removed from the kind of situation the regulation would reach, even assuming it to be a proper construction of the statute. A stipend for studies or research has in the past been disqualified for scholarship treatment because a grantee has performed the function of a paid employee of the grantor, *e.g.*, *Ethel M. Bonn*, 34 T.C. 64 (1960); conversely, a stipend has qualified where a grantee's services "may supplement those of employees of the Institute [connected with the university grantor] but are of themselves not of primary or material benefit to the Institute . . . ." *Wrobleski* v. *Bingler*, 161 F. Supp. 901, 905 (W. D. Pa. 1958).

In the instant case, however, the Government contends that the grantee's research brings his stipend within the reach of Treas. Reg. § 1.117-4(c)(2) (1956), not because it was primarily of direct benefit to Westinghouse and not to the grantee, but rather because it primarily furthered the education and training of the recipient *qua* Westinghouse employee, and as a corollary redounded to the benefit of Westinghouse by enhancing its engineering program in the competitive market for recruits. Even assuming, arguendo, the truth of this contention and the validity of the touchstone of 'primary purpose', nevertheless such indirect advantage as is here alleged has been, and still is, beyond the scope of the regulation.

In summary, we think that the characteristics of what

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[5] This we think is true on analysis, despite the cursory attempt to distinguish *Evans* on this point, in Rev. Rul. 65-146, 1965-1 Cum. Bull. 66.

constitutes a scholarship or fellowship grant for the purposes of the Internal Revenue Code are far from clear. The legislative and judicial gloss provides no sure elucidation, *cf. Reese, supra* at 412. *Compare, e.g., Woddail* v. *Commissioner,* 321 F.2d 721 (10th Cir. 1963) (resident physician receiving residence training in neurology and psychiatry; grant for instruction held taxable) *with Evans, supra* (registered nurse enrolled in psychiatric nursing program on stipend from Tennessee Department of Mental Health for which she will work or to which she will refund stipend; held not taxable).

To us, the nature of the grants here involved is not such as to deprive them of the normal characteristics associated with scholarships or fellowship grants. The single most important purpose that Congress had in mind in enacting § 117 appears through the language of the statute and the Congressional committee reports as that of encouraging financial aid to studies and research, with a preference for the work of degree candidates. In the light of this overriding Congressional goal of encouraging scholarship aid and the accompanying lack of restrictions as to its amount or character in the case of degree candidates, we believe, upon due consideration, that appellants' educational grants do qualify for income tax purposes as excludable scholarships or fellowship grants.

The facts of this case were not in dispute; no question of credibility was presented; no sufficient ground for inconsistent inference of fact was left. As our previous discussion indicates, this case turned on a question solely of statutory construction, requiring only judicial exegesis. Hence the issue below should not have been submitted to the jury, *see Jopek* v. *New York Central R.R.,* 353 F.2d 778, 783 (3d Cir. 1965); *Kocher* v. *Creston Transfer Co.,* 166 F.2d 680, 687 (3d Cir. 1948); *Joseph* v. *United Workers Ass'n,* 343 Pa. 636, 639 (1942).

The judgment of the district court will be reversed and the case remanded for proceedings not inconsistent with this opinion.

A True Copy:

Teste:

Clerk of the United States Court of Appeals for the Third Circuit.

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

Nos. 16,826 to 16,828

RICHARD E. JOHNSON and BEVERLY P. JOHNSON, his wife, and MARTIN L. POMERANTZ and PHYLLIS L. POMERANTZ, his wife, and RICHARD A. WOLFE and ANNE F. WOLFE, his wife

v.

JOHN H. BINGLER, Dist. Director of Internal Revenue

RICHARD E. JOHNSON and BEVERLY P. JOHNSON, his wife, Appellants in No. 16826

MARTIN L. POMERANTZ and PHYLLIS L. POMERANTZ, his wife, Appellants in No. 16827

RICHARD A. WOLFE and ANNE F. WOLFE, his wife, Appellants in No. 16828

(D. C. Civil Action No. 65-1033)

On Appeal From the United States District Court for the Western District of Pennsylvania

Present: HASTIE, *Chief Judge*, GANEY, *Circuit Judge*, and WEINER, *District Judge*.

Judgment

This cause came on to be heard on the record from the United States District Court for the Western District of Pennsylvania and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this Court that the judgment of the said District Court, filed December 2, 1966, be, and the same is hereby reversed and the cause remanded for proceedings not inconsistent with the opinion of this Court.

ATTEST:

THOMAS F. QUINN
Clerk

June 5, 1968

SUPREME COURT OF THE UNITED STATES

No. 473, October Term, 1968

JOHN H. BINGLER, District Director of Internal Revenue,
Petitioner,

v.

RICHARD E. JOHNSON, ET AL.

Order Allowing Certiorari—Filed November 18, 1968.

The petition herein for a writ of certiorari to the United States Court of Appeals for the Third Circuit is granted, and the case is placed on the summary calendar.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

☆ U. S. GOVERNMENT PRINTING OFFICE 1968—331-749/P.O. 450

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In the Supreme Court of the United States

OCTOBER TERM, 1968

No. ——

JOHN H. BINGLER, DISTRICT DIRECTOR OF INTERNAL REVENUE, PETITIONER

v.

RICHARD E. JOHNSON, ET AL.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

The Solicitor General, on behalf of John H. Bingler, District Director of Internal Revenue, petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Third Circuit in these cases.

OPINIONS BELOW

The district court's instructions to the jury are not officially reported. They are unofficially reported at 19 A.F.T.R. 2d 426. The opinion of the court of appeals (Appendix B, *infra,* pp. 5a–17a) is not yet officially reported. It is unofficially reported at 21 A.F.T.R. 2d 1418.

JURISDICTION

The judgment of the court of appeals (Appendix B, *infra,* pp. 18a–19a) was entered on June 5, 1968.

The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATUTE AND REGULATIONS INVOLVED

The relevant provisions of the Internal Revenue Code of 1954 and of the Treasury Regulations on Income Tax (1954 Code) are set forth in Appendix A, *infra*, pp. 1a–3a.

QUESTION PRESENTED

Whether amounts, measured by prior salary and family size, paid by Westinghouse Electric Corporation to selected employees to whom Westinghouse had granted an educational leave of absence for the purpose of completing a doctoral dissertation, and who were obligated to continue in Westinghouse's employ for at least two years after the leave, are excludable from the recipient's gross income as a "scholarship" or "fellowship" within the purview of Section 117 of the Internal Revenue Code of 1954?

STATEMENT

Respondents[1] were employees of the Bettis Atomic Power Laboratory in Pittsburgh, Pennsylvania, which Westinghouse Electric Corporation operates under a cost plus contract with the Atomic Energy Commission (R. 95a–96a).[2] Each respondent partici-

[1] Messrs. Johnson, Pomerantz and Wolfe are referred to herein as "respondents". Their wives are parties solely because joint tax returns were filed for the years in question.

[2] "R.***a" refers to the appendix to respondents' brief in the court of appeals. "R.***b" refers to the appendix to the government's brief in that court. "Tr." refers to the trial transcript.

pated in the Westinghouse Bettis Fellowship and Doctoral Program, one of a variety of training programs that Westinghouse offers to its employees (Tr. 226). This particular program is limited to engineers employed at the Bettis Laboratory who wish to seek a Ph. D. in mechanical or metallurgical engineering at either the University of Pittsburgh or Carnegie Institute of Technology (R. 78a–79a, 95a; Tr. 33, 124, 227–229). The program is funded primarily by the AEC under its general contract for the operation of the Bettis Laboratory (Tr. 236). Officials of Westinghouse and the AEC testified at trial that because of a severe shortage of qualified nuclear scientists and engineers, the Bettis Doctoral program was established in about 1956 to attract engineers and scientists and to aid in meeting the needs of Westinghouse for key professional personnel (R. 78a, Tr. 154, 155, 219). To the date of trial, approximately 60 Westinghouse employees had obtained doctorates through the Bettis program (Tr. 222).

Bettis engineers who participate in the program first enter a "work-study" phase, when they work full time at Westinghouse and study part time[3] at either the University of Pittsburgh or Carnegie Institute of Technology (R. 79a–85a). Those who thereby complete all preliminary requirements for a doctorate—*i.e.*, course work, language studies, and qualification examinations—may apply for an "educational" leave

[3] Westinghouse allows its employees up to eight hours per week (up to 156 hours each year) of paid "released time" in which to attend classes (R. 82a, 83a).

of absence in which to complete a dissertation. Each applicant—and the topic of his proposed thesis—must be approved by Westinghouse and by the AEC (R. 4b, 5b, 12b–15b, Tr. 228–229, 273–276). Strict controls are employed to ensure the relationship of thesis topics to the work program of the laboratory (R. 4b, 5b, 12b–15b, Tr. 228–229, 273–276). Those selected must agree to work at Bettis for at least two years after completion of the leave (R. 90a–91a, Tr. 32, 33; Defendants' Exhibits 1, 3, Tr. 63, 119). While on educational leave an engineer receives a so-called "living stipend"—a fixed percentage of his prior salary at Westinghouse plus amounts that depend on the size of his family, up to a fixed maximum (R. 87a, 88a).

Westinghouse's internal records designate those on educational leave of absence as employees of the Bettis Laboratory. The "living stipends" are charged to the indirect labor overhead of the laboratory, and Westinghouse treats these amounts as wages for withholding and Social Security tax purposes (R. 7b, 8b). Those on leave retain their seniority status (Tr. 253, 254) and receive all employee benefits, such as hospitalization, insurance, and stock option privileges (R. 5b). They continue to contribute to and accumulate rights under the Westinghouse pension plan—and they are eligible for vacation immediately upon return from leave (R. 5b).

After successfully completing the work-study phase of the Bettis program, each of the three respondents was granted a leave of absence for the purpose of pursuing thesis topics that Westinghouse and the

AEC had approved. During leaves of nine months, respondents Johnson[4] and Pomerantz[5] were each paid $5,670, representing 80% of their prior salaries at Westinghouse. Respondent Wolfe, whose leave lasted a year,[6] received $9,698.90, which amounted to 90% of his prior salary (Tr. 30, 31, 32).

Westinghouse withheld income tax from these amounts. Respondents filed claims for refund, contending that the payments were excludable from gross income as scholarships under Section 117 of the Internal Revenue Code of 1954 (Appendix A, p. 1a–2a). The Commissioner of Internal Revenue rejected these claims, and timely refund suits were brought in the district court.

At a consolidated trial, the court instructed the jury that:

> amounts of money or stipends paid to an individual to enable him to pursue studies or research are considered to be amounts received as a scholarship or fellowship grant if the primary purpose of the studies or research is to further the education and training of the recipient in his individual capacity * * *. [R. 61a.]

The instructions continued, however, to say that a scholarship or fellowship does not include an amount that either represents "compensation for past, pres-

[4] Respondent Johnson was on leave from October 1, 1960 to June 30, 1961 (Tr. 30).

[5] Respondent Pomerantz was on leave from November 1, 1961 to July 31, 1962 (Tr. 31).

[6] Respondent Wolfe was on leave from March 1, 1960 to February 28, 1961 (Tr. 31).

ent or future employment services, or represents payments for services which are subject to the direction or supervision of the grantor" or are "paid to an individual to enable him to pursue studies or research which studies or research are primarily for the benefit of the grantor * * *." (R. 61a, 62a.)

In answer to special interrogatories, the jury found that the amounts received by each respondent from Westinghouse did not constitute excludable scholarships or fellowships (R. 96a). Judgment accordingly was entered in favor of the District Director.

On appeal the Court of Appeals for the Third Circuit reversed, holding that the amounts paid to respondents during their educational leaves of absence were excludable, and that the issue should not have been submitted to the jury.[7] The court reasoned that even if a payment had "'indicia of compensation'", it could nonetheless be characterized as an excludable scholarship. Accordingly, the court disapproved (App. B, p. 10a) the provision of Treasury Regulation § 1.117–4(c)(1), which states that Section 117 does not encompass amounts that represent (App. A, p. 3a) "compensation for past, present, or future employment services." It also ruled that the amounts paid respondents were not compensation for future employment at Westinghouse, since respond-

[7] Because respondents did not move for either a directed verdict or judgment n.o.v. at trial, we interpret the decision below as calling for a new trial and not the entry of judgment for respondents. See, *Globe Liquor Co.* v. *San Roman*, 332 U.S. 571; *Cone* v. *West Virginia Paper Co.*, 330 U.S. 212; *Johnson* v. *New York, N.H. & H.R. Co.*, 344 U.S. 48, 54 n. 3.

ents, after completing their doctorates, were to be paid at a rate commensurate with their then education and experience. Finally, the court held (App. B, pp. 14a–16a), that whatever "indirect advantage" the Bettis program gave Westinghouse was beyond the scope of Regulation Section 1.117–4(c)(2), which states that amounts "paid or allowed to * * * an individual to enable him to pursue studies or research primarily for the benefit of the grantor" are not a "scholarship" or "fellowship".

REASONS FOR GRANTING THE WRIT

1. The decision of the Third Circuit in this case is in conflict with decisions of the Courts of Appeal for the Fifth and Sixth Circuits and of the Court of Claims. In *Ussery* v. *United States*, 296 F. 2d 582, the Fifth Circuit held that Section 117 did not allow a taxpayer to exclude from gross income monthly stipends he received from the Mississippi Department of Public Welfare, which had granted him educational leave while he secured his Master's Degree in social work, and to whose employ he was required to return upon completion of his studies. In sustaining Section 1.117–4(c)(2) of the Regulations as a reasonable interpretation of the statute, the court reasoned (296 F. 2d at 586) "that the terms 'scholarship' and 'fellowship' were used as opposed to a term such as 'compensation' and were carefully selected to bar cases where a payment is made for work primarily for the benefit of the grantor." The payments in question were held to fall within the barred category, because the purpose of the program was to train employees

so that they could benefit the Department of Welfare by performing their duties more effectively (*ibid.*).

Stewart v. *United States*, 363 F. 2d 355 (C.A. 6), concerned a taxpayer who received an educational leave and grant from the Tennessee Department of Public Welfare to pursue a Master's Degree in social work. The Sixth Circuit ruled that the payments were includable in gross income because various "indicia of compensation"—such as a contractual obligation to return to the employ of the Department upon completion of leave, and the retention of civil service status and retirement and other fringe benefits—made the payments such "compensation for past, present, or future services" as Section 1.117-4(c)(1) of the Regulations excludes from the definition of "scholarship" and "fellowship".

In like manner, the Court of Claims decided in *Reiffen* v. *United States*, 376 F. 2d 883, that gross income must include amounts paid to an employee of MIT's Lincoln Laboratory who was assigned no work responsibility during an eight month period while he was a full time graduate student, completing research and other requirements for a Ph. D. in electrical engineering. Because the primary purpose of the program was to enable Lincoln to compete with industry and other organizations in the recruitment and retention of scientific and professional personnel, the court, resting on and approving Regulation Section 1.117-4(c), held that Lincoln's payments were made to

enable the engineer to pursue studies and research primarily for the benefit of Lincoln.[8]

2. The Third Circuit has incorrectly construed the statute and unjustifiably rejected the interpretation set forth in the pertinent Treasury Regulation. The decisions of the Fifth and Sixth Circuits and the Court of Claims are correct.

Prior to 1954, no statutory provision explicitly dealt with scholarships and fellowships. The policy of the Internal Revenue Service was founded on the general terms of Sections 22(a) and 22(b)(3) of the 1939 Code. Thus the Service concluded that an amount labeled "scholarship" or "fellowship" would fall within the all-encompassing definition of "gross income" in Section 22(a) unless it qualified as a "gift" within the meaning of Section 22(b)(3). See I. T. 4056, 1951–2 Cum. Bull. 8.

With a view to alleviating the difficulties of a rule that required a case-by-case inquiry into the question whether a "gift" was intended,[9] Congress wrote Sec-

[8] The decision below is also at odds with the reasoning of *Woddail* v. *Commissioner*, 321 F. 2d 721, 724 (C.A. 10) (gross income includes money the Veterans Administration paid a resident in psychiatry and neurology who promised to remain a Veterans Administration employee for a specified time for each year of resident training, because "it was an amount paid for services and was primarily for the benefit of the grantor"), and *Reese* v. *Commissioner*, 373 F. 2d 742 (C.A. 4), affirming *per curiam* 45 T.C. 407 (taxpayer failed to show that $1,900 received while teaching to satisfy a requirement for a master's degree was paid primarily to further her education rather than to compensate her for services rendered).

[9] Compare *Ti Li Loo* v. *Commissioner*, 22 T.C. 220, and *Evens* v. *Commissioner*, 1961 T.C.M. 179, with *Stone* v. *Commissioner*, 23 T.C. 254.

tion 117 into the 1954 Code. (H. Rep. No. 1337, 83d Cong., 2d Sess. 16; S. Rep. No. 1622, 83d Cong., 2d Sess. 17). Section 117(a) states that "gross income does not include * * * any amount received * * * as a scholarship * * * or * * * as a fellowship grant * * *." There is not, however, any statutory definition of the words "scholarship" and "fellowship".

Scholarships and fellowships are, of course, amounts paid to support a student or scholar while he is pursuing studies or independent research, and this is the position taken in the relevant Treasury Regulations. See Treas. Regs §§ 1.117–3(a) and (c). It is equally clear, on the other hand, that a payment is not a scholarship or fellowship merely because it contributes to the support of a student or researcher. At the very least, as the court of appeals recognized in the present case (App. B, pp. 13a–14a):

> A significant commitment by the student in return for a grant would, of course, place that grant outside the category "scholarship", at least to the extent of the value of that commitment. For if the grantee had to barter for his stipend, giving full value for it, this arrangement would hardly serve the primary purpose of the § 117 exclusion: to encourage financial aid to education through tax relief.

To the extent that Congress could foresee such arrangements it expressly forbade or limited the tax exemption. Section 117(b)(1) specifically provides that the "scholarship" exclusion does not apply to payments made for teaching, research, or other services in the nature of part time employment required

as a condition to receiving the grant. The committee reports expressed an intention to tax grants that are, in effect, merely continuing salary payments to non-degree candidates while on leave from a regular job. H. Rep. No. 1337, 83d Cong., 2d Sess., 16–17; S. Rep. No. 1622, 83d Cong., 2d Sess., 17–18. Accordingly, non-degree candidates are allowed to exclude from gross income only grants paid by governmental agencies or charitable, educational and other tax-exempt "organizations described in Section 501(c)(3)," and then only in the amount of $300 for each month of the grant's duration, for a maximum of three years. See Section 117(b)(2).

The thrust of the legislation is clear: Generally speaking, amounts paid for the support of a scholar constitute an excludable scholarship or fellowship. On the other hand, amounts that relate to the provision of services or some other *quid pro quo* by the recipient must be included in gross income. Accordingly, the regulations carve out two basic exceptions from the general definition of excludable scholarships and fellowships cited above: tax exempt treatment is denied (Treas. Reg. § 1.117–4(c), App. A, p. 3a) to amounts that represent either "compensation for past, present, or future employment services," or amounts that finance education or research that is undertaken primarily for the benefit of the grantor.

These regulations, which four circuits and the Court of Claims have sustained,[10] are plainly reasonable "contemporaneous constructions by those charged with administration of these statutes which should

[10] See cases cited pp. 7–9 and footnote 8, *supra*.

not be overruled except for weighty reasons." *Commissioner* v. *South Texas Co.*, 333 U.S. 496, 501. Their obvious purpose and effect is to deny tax exemption to payments that are essentially compensatory, which accords with the statutory scheme and is in keeping with the ordinary meaning of "scholarship" and "fellowship." "Although study or research undertaken in an educational program may be of benefit to a grantor, the terms 'scholarship' and 'fellowship' connote a purpose of assistance that stands in distinction to the self-interest of an employer in the compensation of his employee." (*Ussery* v. *United States*, *supra*, 296 F. 2d at 585). There is, in consequence, no basis for the Third Circuit's action in overturning (App. B. p. 10a) Section 1.117–4(c)(1) and refusing to apply (App. B, pp. 14a–15a) Section 1.117–4(c)(2) of the Regulations in the manner its words plainly require.

By any of these standards, Westinghouse's payments to respondents should fail to qualify for exclusion from taxation. The opportunity to obtain a doctorate while supported by Westinghouse was part of the overall package of salary and fringe benefits for which respondents bargained when they first entered into Westinghouse's employ (Tr. 115). Working for Westinghouse during the work-study phase was the first requirement of the later, paid leaves of absence. Contrary to the Third Circuit's view (App. B, p. 13a–14a) that respondents made no "significant commitment" and provided nothing "of measurable monetary value," Westinghouse paid so-called "stipends"

on the basis of respondents' commitments to work for two additional years, and the choice of thesis topics that fit into the overall research program of the Bettis Laboratory. The payments were simply continuing salary payments to an employee who was granted leave so that he might upgrade skills required by Westinghouse, requirements that Westinghouse otherwise could not have fulfilled. Westinghouse avoided the need to recruit new people, and respondents surrendered their freedom of choice of employers for a significant period of time. The jury, we submit, had no choice but to find for the government on this record; at the very least the court of appeals should have left standing the jury verdict, which denied tax exemption on the basis of instructions that where substantially in accord with the Treasury's Regulation.

3. Although the exact number of such programs is not known, there are many employers who allow selected employees paid leaves of absence to complete a graduate degree, exacting in return some commitment to return to the employer for a specified minimum period. Companies engaged in advanced technical research and development must offer such benefits if only to compete. Cf. *Reiffen* v. *United States*, *supra*, 376 F.2d at 886. As *Ussery* and *Stewart* demonstrate, these paid leaves of absence are restricted neither to private employers nor to technical personnel.

The Internal Revenue Service has advised us that there are at least 40 pending matters involving the

tax status of payments received by an employee while on educational leave. Many more are sure to arise if the issue is not conclusively settled. For example, in fiscal 1967 alone, more than 500 employees of the United States were allowed paid, educational leaves of absence of one semester or more. The tax rules to be applied to persons in such circumstances will remain unsettled and the Internal Revenue Service and the courts will be unable to accord like treatment to similarly situated taxpayers unless this Court grants certiorari and resolves the uncertainty created by the decision below.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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SEPTEMBER 1968.

APPENDIX A

Internal Revenue Code of 1954:

SEC. 117. SCHOLARSHIPS AND FELLOWSHIP GRANTS.

(a) *General Rule.*—In the case of an individual, gross income does not include—

(1) any amount received—

(A) as a scholarship at an educational institution (as defined in section 151(e)(4)), or

(B) as a fellowship grant,

including the value of contributed services and accommodations; and

(2) any amount received to cover expenses for—

(A) travel,

(B) research,

(C) clerical help, or

(D) equipment,

which are incident to such a scholarship or to a fellowship grant, but only to the extent that the amount is so expended by the recipient.

(b) *Limitations.*—

(1) *Individuals who are candidates for degrees.*—In the case of an individual who who is a candidate for a degree at an educational institution (as defined in section 151(e)(4)), subsection (a) shall not apply to that portion of any amount received which represents payment for teaching, research, or other services in the nature of part-time employment required as a condition to receiving the scholarship or the fellowship grant. If teaching, research, or other services are required of all candidates (whether or not recipients of scholarships or fellowship grants) for a particular degree as a condition to receiving such degree, such teaching, research, or other

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services shall not be regarded as part-time employment within the meaning of this paragraph.

(2) *Individuals who are not candidates for degrees.*—In the case of an individual who is not a candidate for a degree at an educational institution (as defined in section 151(e)(4)), subsection (a) shall apply only if the condition in subparagraph (A) is satisfied and then only within the limitations provided in subparagraph (B).

(A) *Conditions for exclusion.*

The grantor of the scholarship or fellowship grant is—

(i) an organization described in section 501(c)(3) which is exempt from tax under section 501(a),

(ii) a foreign government,

(iii) an international organization, or a binational or multinational education and cultural foundation or commission created or continued pursuant to the Mutual Educational and Cultural Exchange Act of 1961, or

(iv) the United States, or an instrumentality or agency thereof, or a State, a territory, or a possession of the United States, or any political subdivision thereof, or the District of Columbia.

(B) *Extent of exclusion.*—The amount of the scholarship or fellowship grant excluded under subsection (a)(1) in any taxable year shall be limited to an amount equal to $300 times the number of months for which the recipient received amounts under the scholarship or fellowship grant during such taxable year, except that no exclusion shall be allowed under subsection (a) after the recipient has been entitled to exclude under this section for a period of 36 months (whether or not consecutive) amounts received as a scholarship or fellowship grant while not a candidate for a degree at an educational institution (as defined in section 151(e)(4)).

[26 U.S.C. 1964 ed., Sec. 117]

Treasury Regulations on Income Tax (1954 Code):

§ 1.117–4 *Items not considered as scholarships or fellowship grants.*

The following payments or allowances shall not be considered to be amounts received as a scholarship or a fellowship grant for the purpose of section 117:

* * * * *

(c) *Amounts paid as compensation for services or primarily for the benefit of the grantor.* (1) Except as provided in paragraph (a) of § 1.117–2, any amount paid or allowed to, or on behalf of, an individual to enable him to pursue studies or research, if such amount represents either compensation for past, present, or future employment services or represents payment for services which are subject to the direction or supervision of the grantor.

(2) Any amount paid or allowed to, or on behalf of, an individual to enable him to pursue studies or research primarily for the benefit of the grantor.

However, amounts paid or allowed to, or on behalf of, an individual to enable him to pursue studies or research are considered to be amounts received as a scholarship or fellowship grant for the purpose of section 117 if the primary purpose of the studies or research is to further the education and training of the recipient in his individual capacity and the amount provided by the grantor for such purpose does not represent compensation or payment for the services described in subparagraph (1) of this paragraph. Neither the fact that the recipient is required to furnish reports of his progress to the grantor, nor the fact that the results of his studies or research may be of some incidental benefit to the grantor shall, of itself, be considered to destroy the essential character of such amount as a scholarship or fellowship grant. [26 C.F.R., Sec. 1.117–4.]

APPENDIX B

United States Court of Appeals for the Third Circuit

Nos. 16826, 16827 and 16828

RICHARD E. JOHNSON AND BEVERLY P. JOHNSON, HIS WIFE, AND MARTIN L. POMERANTZ AND PHYLLIS L. POMERANTZ, HIS WIFE, AND RICHARD A. WOLFE AND ANNE F. WOLFE, HIS WIFE

v.

JOHN H. BINGLER, DISTRICT DIRECTOR OF INTERNAL REVENUE

RICHARD E. JOHNSON AND BEVERLY P. JOHNSON, HIS WIFE, APPELLANTS IN NO. 16826

MARTIN L. POMERANTZ AND PHYLLIS L. POMERANTZ HIS WIFE, APPELLANTS IN NO. 16827

RICHARD A. WOLFE AND ANNE F. WOLFE, HIS WIFE, APPELLANTS IN NO. 16828

Appeal From the United States District Court for the Western District of Pennsylvania

Argued January 18, 1968

Before HASTIE, *Chief Judge*, GANEY, *Circuit Judge*, and WEINER, *District Judge*.

OPINION OF THE COURT

(Filed June 5, 1968)

By WEINER, *District Judge*:

Before us on this appeal are three taxpayers [1] who, while employees of the Westinghouse Electric Cor-

[1] Appellants' wives are joined as nominal plaintiff-appellants by virtue of the joint income tax returns filed by them with their husbands for the years involved.

poration, were participants in the Westinghouse Bettis Fellowship and Doctoral Program through which each received a stipendiary grant and leave of absence from his employer in order to research, write, and defend his Ph.D. thesis in engineering at either the University of Pittsburgh or Carnegie Institute of Technology (now Carnegie-Mellon University).

There was testimony below that the Bettis Atomic Power Laboratory, at which each taxpayer was employed before and after his academic leave of absence, is owned by the United States Government and is operated by Westinghouse under a "cost-plus" type of contract with the Atomic Energy Commission. Appellants' theses related to the work program of the Laboratory in the field of nuclear engineering.

Income tax was withheld from the monthly allowances received by each of the three appellants; each filed a claim for refund of this tax on the grounds that the grant was excludable from his gross income as a scholarship under Int. Rev. Code of 1954, § 117. These claims were rejected by the Internal Revenue Service, and again by a jury in the trial below.

The correctness of this determination is the subject of this appeal.

The crucial terms "scholarship" and "fellowship grant" appear in the relevant § 117 without any definition whatsoever.[2] In the absence of any guidance

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[2] In pertinent part, § 117(a)(1) provides as follows:

"(a) General rule.—In the case of an individual, gross income does not include—

(1) any amount received—

(A) as a scholarship at an educational institution (as defined in section 151(e)(4)), or

(B) as a fellowship grant. . . ."

26 U.S.C. § 117(a)(1).

as to the content of these statutory concepts embodied in the Code itself, we agree with the Tax Court that—

> a proper reading of the statute requires that before the exclusion comes into play there must be a determination that the payment sought to be excluded has the normal characteristics associated with the term "scholoraship."

Elmer L. Reese, Jr., 45 T.C. 407, 413 (1966), *aff'd per curiam*, 373 F.2d 742 (4th Cir. 1967). Without attempting a comprehensive definition, we can simply mention some of the more salient "normal characteristics" of such scholarships or fellowship grants that are exemplified in the situation before us.

Appellants' stipends were awarded as subsidies to full-time students, in an amount bearing an appropriate relation to each recipient's needs. Their continuance was contingent upon the participant's maintenance of the academic standards required of a candidate for a graduate degree by the university which each appellant attended. While receiving these grants, appellants were on an academic leave of absence from their employment for the specific purpose of completing their doctoral dissertations. These are the most important positive characteristics which appellants' grants shared with scholarships generically. We turn now to the Code and the legislative history for an understanding of the distinctions with which Congress intentionally colored the kind of grant it wished excluded from gross income for internal revenue purposes.

Most notable in the legislative tax treatment of scholarships is that the Congress in 1954 was painting with a broad brush. Grants which properly qualify as scholarships are excluded from taxation in very unqualified terms by § 117(a). In the case of candidates for a degree, such as appellants before us, this exclu-

sion is explicitly limited in the statute only as not applying—

> to that portion of any amount received which represents payment for teaching, research, or other services in the nature of part-time employment, required as a condition to receiving the scholarship or fellowship grant.

Int. Rev. Code of 1954, § 117(b)(1). The statute as it applies to degree candidates provides no ceiling for the amount that the candidate may exclude from his gross income, as long as it otherwise properly qualifies for scholarship tax treatment. This is in sharp contradistinction to the limit of $300 a month for a maximum of 36 months to which those not candidates for a degree are held. *Compare* § 117(b)(1) *with* § 117(b)(2)(B).

The legislative history also evinces unmistakably the intent of Congress to exclude from tax treatment qualifying scholarships without regard to whether they are to be considered "as income or as gifts," H.R. Rep. No. 1337, 83d Cong., 2d Sess. 15 (1954), as had been the test hitherto applied under the then "existing confusion," *id.*, for which the 1954 change was an attempted remedy. The Senate Report, furthermore, carefully sets out the sequence of the thinking that went into § 117:

> The section first states the general rule that amounts received as scholarships or as fellowship grants are excludible from gross income and then prescribes specific rules for limiting the amounts which may be excluded.

S. Rep. No. 1622, 83d Cong., 2d Sess. 17 (1954).

In light of the statutory language and the reports of the Congressional committees which drafted it, the dominant legislative intent evident in the scheme of § 117 is that of encouraging financial aid to students at accredited schools, and especially to candi-

dates for degrees, through the device of limited tax relief. The further attention given by both the statute and the legislative history[3] toward limiting the exclusion only for those *not* candidates for a degree would strengthen the inference, by the canon of statutory construction that *expressio unius est exclusio alterius,* that Congress intentionally included the sole restrictions it wished to place on the excludability of scholarship stipends for degree candidates in the language of § 117(b)(1) itself.

To the sole qualification of § 117(b)(1), then, that degree candidates cannot exclude as tax-exempt scholarships any payment for services required as a condition of the grant, the Treasury Regulations purport to add two others. These would subject to taxation, in pertinent part, any stipend for studies or research which (1) "represents either compensation for past, present, or future employment services"; or which (2) subsidizes studies or research "primarily for the benefit of the grantor." Treas. Reg. 1.117-4(c)(1)-(2), (1956).

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[3] H.R. Rep. No. 1337, *supra* at 17 expressed concern, in the case of non-degree candidates, lest the exclusion extent to any annual grant which, together with "any compensation received from the recipient's previous employer," exceeded 75% "of the recipient's salary in the year preceding the grant." In taxing any amount above this limit, the House committee declared: "This will tax those grants which are in effect merely payments of a salary during a period while the recipient is on leave from his regular job." *Id.* For this percentage exclusion the Senate committee "substituted for the 75 percent rule an exclusion of $300 per month of grants paid to individuals who are not candidates for degrees." S. Rep. No. 1622, *supra* at 18. Both committees evidently foresaw the instant problem and legislated with respect to the type of student and the amount of stipend they wished to subject to a limitation on excludability.

In light of the aim explicit in the legislative history of doing away with the touchstone of compensation versus gift, we cannot say, as one court has, that "indicia of compensation' such as are suggested by the regulation are legitimate criteria for testing the excludability of an alleged scholarship, *cf. Stewart* v. *United States,* 363 F. 2d 355, 357 (6th Cir. 1966). Nor can we even approve the disqualification added by Treas. Reg. § 1.117–4(c)(1) (1956) of amounts which represent "compensation for past, present, or future employment services," without more. *Contra, Ussery* v. *United States,* 296 F. 2d 582, 586–87 (5th Cir. 1961). This ruling seems merely an attempt to write into the regulations a concept which was considered and intentionally rejected by the Congress which enacted the Code.

To summarize: under a fair reading of the Internal Revenue Code of 1954, § 117, in the light of the Congressional committee reports which point up the thinking of the 1954 Congress, we believe that any reasonable stipend which comes within the common understanding of what constitutes a scholarship, is paid to finance the schooling of a degree candidate, and does not fall within the limitation of § 117(b)(1) is excluded from gross income. To illustrate the application of this general outline, we shall take up the Government's arguments in the discussion remaining.

The first element in the Westinghouse Fellowship Program that appears to trouble the Internal Revenue Service is the fact that each grant for those recipients on educational leave was based on a percentage of the grantee's "base salary".[4] The basis on which each

[4] Depending on the family status of the recipient, a Westinghouse Fellow received a stipend of 70% "of the base salary" plus "adders" up to a monthly maximum of $490 if single; 80% plus adders up to $560 monthly if married; 85% plus

Westinghouse Fellowship grant was calculated was, however, not without some logic other than as what might arguably be a disguised salary payment. Scholarships are characteristically based at least partly on need, and the Westinghouse grants were calculated, perhaps generously, to give each recipient a living allowance based upon the size of his family and the standard of living to which his previous salary had accustomed him, without a sudden substantial cut in revenue. Monthly maxima were set; these ceilings do not appear to us to have been excessive or unreasonable—the one limitation most probably implicit in the otherwise unrestricted excludability of scholarships for degree candidates in § 117.

The concept and content of "scholarship" are developing ones. Fundamental in the exclusion afforded such stipends by § 117 is its encouragement toward graduate study. Without an arrangement of subsidies on a sliding scale based on prior income, employees such as appellants here would probably be hard pressed to leave work for a year to return to school to earn an advanced degree. We think the purpose of the instant fellowship program entirely consistent as concerns appellant degree candidates with the scheme of the exclusion afforded scholarships by the Internal Revenue Code of 1954, § 117. There is, moreover, as we have noted above, no ceiling to this exclusion in the statute.

Although the Senate report on § 117 did not discuss the problem of salary payments disguised as educational stipends for degree candidates, it did display concern for this problem with regard to postdoctoral students. In this connection, it notes: "Such grants

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adders up to $595 monthly if married with one child; and 90% plus adders up to $630 if married with two or more children.

may be in effect a continuing salary payment while the recipient is on leave from his regular job," S. Rept. No. 1622, *supra* at 18. The preventive response of Congress, however, was restricted to the $300 monthly limit of § 117(b)(2)(B) for nondegree candidates.

Hence the Westinghouse grants, even based as they were partly on a percentage of each recipient's prior earnings and partly on family size and need, do not seem to us for this reason to disqualify for exclusion either under the statutory language or because of any alleged failure to meet what we consider to be "the normal characteristics associated with the term 'scholarship'."

The second reason advanced by the Government for disqualifying these grants from nontaxable scholarship treatment is that the grantor, Westinghouse, in its own bookkeeping did not denominate them as such: it carried them, rather, as "indirect labor, or overhead." Deductions from the stipend checks, moreover, were regularly made for income tax and social security payments. An evident discrepancy exists between the characterization of these grants both by appellants and by the Fellowship prospectus as "stipends", on the one hand, and by the custodian of the payroll records at the Westinghouse Bettis Atomic Power Laboratory as "indirect labor", on the other.

The answer to this contention by the Government that the grantor's treatment controls, however, has already been given by this circuit in a similar case, where we recently had occasion to—

> observe and emphasize that under this regulation [§ 1.117-4(c)(2)(1956)] the determinative consideration is not the primary purpose of the grantor in subsidizing the student, but rather the primary purpose of and the primary benefit from the subsidized study.

Commissioner v. Ide, 335 F.2d 852, 855 (3d Cir. 1964) (Hastie, J.). Although the court in *Ide* was considering more particularly the taxability of the grants there in question on the grounds that the work done by the grantees was "primarily for the benefit of the grantor," in the words of Treas. Reg. § 1.117–4(c)(2) (1956); nonetheless we believe this observation equally valid as a caution against grafting an additional subjective test based on the grantor's intention onto the existing statutory language which was intended to obviate this inquiry. *Accord, Chandler P. Bhalla,* 35 T.C. 13, 17 (1960) (by implication), *acquiesced in,* 1965–1 Cum. Bull. 4.

The third element of this program to which the Internal Revenue Service objects is the commitment required by the Westinghouse Bettis Fellowship and Doctoral Programs of each participating fellow:

> that after the end of his educational leave he will assume such duties commensurate with his education and experience as may be assigned to him by Westinghouse, and will thereafter continue in the employ of Westinghouse for at least two (2) calendar years at a rate of salary commensurate with the duties assigned.

We do not agree with the Government that this commitment, in this case, is sufficient evidence that these stipends were of an essentially "compensatory nature". Compensation for the future "duties" of each grantee is to be at a "commensurate" salary, presumably without adjustment downwards to take account of the instant grant.

Assuming the above clause to be unenforceable by specific performance, we think it nonetheless apparent that contingent liability in damages for the breach of such a clause might be of substantial value in an appropriate factual situation. A significant commitment

by the student in return for a grant would, of course, place that grant outside the category "scholarship", at least to the extent of the value of that commitment. For if the grantee had to barter for his stipend, giving full value for it, this arrangement would hardly serve the primary purpose of the § 117 exclusion: to encourage financial aid to education through tax relief.

In the instant situation, however, appellants' promise to return to employment with Westinghouse at an appropriate salary would subject them to no financial sacrifice. They are to be paid in accordance with their enhanced educational qualifications. Since a salary commensurate to their new duties is already inducement for them to return to their employer-grantor, appellants' additional paper commitment seems of negligible value in this case.

We of course express no opinion as to cases where the quid pro quo given by the grantee for his grant is of measurable monetary value.

Viewed in a light most adverse to appellants, their situation is still akin to that in *Aileene Evans*, 34 T.C. 720 (1960), *acquiesced in*, 1965–1 Cum. Bull. 4. There the Tax Court held petitioner's stipend excludable from her gross income under § 117, even though she was obligated either to work for her grantor after her studies or to refund the sums advanced. Although petitioner in *Evans* was not an employee of the grantor at the time she received her stipend, we do not deem this distinction material to the hypothetical question of compensation for future employment services.[5]

The last argument advanced by the Government is that appellants' studies were not primarily for the

[5] This we think is true on analysis, despite the cursory attempt to distinguish *Evans* on this point, in Rev. Rul. 65–146, 1965–1 Cum. Bull. 66.

purpose of educating and training each recipient in his individual capacity, but rather in his capacity as an employee of the grantor. The grants, the Government argues, would hence be proscribed by Treas. Reg. § 1.117–4(c)(2) (1956).

To decide this issue, we do not have to consider the validity of this regulation in the light of the statutory language and legislative history of § 117. For the Government's argument is one step removed from the kind of situation the regulation would reach, even assuming it to be a proper construction of the statute. A stipend for studies or research has in the past been disqualified for scholarship treatment because a grantee has performed the function of a paid employee of the grantor, *e.g., Ethel M. Bonn,* 34 T.C. 64 (1960); conversely, a stipend has qualified where a grantee's services "may supplement those of employees of the Institute [connected with the university grantor] but are of themselves not of primary or material benefit to the Institute . . . ." *Wrobleski v. Bingler,* 161 F. Supp. 901, 905 (W.D. Pa. 1958).

In the instant case, however, the Government contends that the grantee's research brings his stipend within the reach of Treas. Reg. § 1.117–4(c)(2)(1956), not because it was primarily of direct benefit to Westinghouse and not to the grantee, but rather because it primarily furthered the education and training of the recipient *qua* Westinghouse employee, and as a corollary redounded to the benefit of Westinghouse by enhancing its engineering program in the competitive market for recruits. Even assuming arguendo, the truth of this contention and the validity of the touchstone of 'primary purpose', nevertheless such indirect advantage as is here alleged has been, and still is, beyond the scope of the regulation.

In summary, we think that the characteristics of what constitutes a scholarship or fellowship grant for the purposes of the Internal Revenue Code are far from clear. The legislative and judicial gloss provides no sure elucidation, *cf. Reese, supra* at 412. *Compare, e.g., Woddail v. Commissioner,* 321 F.2d 721 (10th Cir. 1963) (resident physician receiving residence training in neurology and psychiatry; grant for instruction held taxable) *with Evans, supra* (registered nurse enrolled in psychiatric nursing program on stipend from Tennessee Department of Mental Health for which she will work or to which she will refund stipend; held not taxable).

To us, the nature of the grants here involved is not such as to deprive them of the normal characteristics associated with scholarships or fellowship grants. The single most important purpose that Congress had in mind in enacting § 117 appears through the language of the statute and the Congressional committee reports as that of encouraging financial aid to studies and research, with a preference for the work of degree candidates. In the light of this overriding Congressional goal of encouraging scholarship aid and the accompanying lack of restrictions as to its amount or character in the case of degree candidates, we believe, upon due consideration, that appellants' educational grants do qualify for income tax purposes as excludable scholarships or fellowship grants.

The facts of this case were not in dispute; no question of credibility was presented; no sufficient ground for inconsistent inference of fact was left. As our previous discussion indicates, this case turned on a question solely of statutory construction, requiring only judicial exegesis. Hence the issue below should not have been submitted to the jury, *see Jopek v.*

New York Central R.R., 353 F.2d 778, 783 (3d Cir. 1965); *Kocher v. Creston Transfer Co.*, 166 F.2d 680, 687 (3d Cir. 1948); *Joseph v. United Workers Ass'n.*, 343 Pa. 636, 639 (1942).

The judgment of the district court will be reversed and the case remanded for proceedings not inconsistent with this opinion.

A True Copy:
Teste:

Clerk of U.S. Court of Appeals
for the Third Circuit.

United States Court of Appeals for the Third Circuit

Nos. 16,826 to 16,828

RICHARD E. JOHNSON AND BEVERLY P. JOHNSON, HIS WIFE, AND MARTIN L. POMERANTZ AND PHYLLIS L. POMERANTZ, HIS WIFE, AND RICHARD A. WOLFE AND ANNE F. WOLFE, HIS WIFE

v.

JOHN H. BINGLER, DISTRICT DIRECTOR OF INTERNAL REVENUE

RICHARD E. JOHNSON AND BEVERLY P. JOHNSON, HIS WIFE, APPELLANTS IN NO. 16826

MARTIN L. POMERANTZ AND PHYLLIS L. POMERANTZ HIS WIFE, APPELLANTS IN NO. 16827

RICHARD A. WOLFE AND ANNE F. WOLFE, HIS WIFE, APPELLANTS IN NO. 16828

(D.C. Civil Action No. 65–1033)

On Appeal From the United States District Court for the Western District of Pennsylvania

Present: HASTIE, *Chief Judge,* GANEY, *Circuit Judge,* and WEINER, *District Judge.*

JUDGMENT

This cause came on to be heard on the record from the United States District Court for the Western District of Pennsylvania and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this Court that the judgment of the

said District Court, filed December 2, 1966, be, and the same is hereby reversed and the cause remanded for proceedings not inconsistent with the opinion of this Court.

Attest:

THOMAS F. QUINN, *Clerk.*

JUNE 5, 1968.

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IN THE

Supreme Court of the United States

October Term, 1968

No. 473

JOHN H. BINGLER, District Director of Internal Revenue,
Petitioner,

v.

RICHARD E. JOHNSON, *et al.*

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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IN THE

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RICHARD E. JOHNSON, *et al.*

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

The respondent taxpayers oppose the Petition of John H. Bingler. District Director of Internal Revenue, for a Writ of Certiorari to review the judgment of the United States Court of Appeals for the Third Circuit in these cases.

Opinions Below

The district court's instructions to the jury are not officially reported. They are unofficially reported at 19 A. F. T. R. 2d 426. The opinion of the court of appeals (Petitioner's Appendix B, pages 5a-17a) is officially reported at 396 F. 2d 258.

Jurisdiction

The grounds on which the jurisdiction of this court is invoked are stated in the Petition for Writ of Certiorari.

Statute and Regulations Involved

The relevant provisions of the Internal Revenue Code of 1954 and of the Treasury Regulations on Income Tax (1954 Code) are set forth in the Petition for Writ of Certiorari, Appendix A, pages 1a-3a.

Question Presented

Whether an employer may make a scholarship grant to an employee (who is a degree candidate at an educational institution) which may be excludable from gross income under Section 117 of the Internal Revenue Code of 1954 without the necessity of establishing such grant as a gift.

Statement

Each of the respondents was an employee of Westinghouse Electric Corporation in Pittsburgh, Pennsylvania, at its Bettis Atomic Power Laboratory.

Westinghouse had initiated a doctoral program which provided employees of the company with the opportunity of securing the degree of Doctor of Philosophy in engineering and science. The program was undertaken in cooperation with the University of Pittsburgh and Carnegie Institute of Technology (now Carnegie-Mellon University) (R-14a).[1]

The respondents were enrolled as students at the respective universities in the same manner and were

(1) "R" refers to the Appendix to Respondents' Brief in the Court of Appeals.

required to meet the same scholastic standards for the degree as other graduate students (R-14a). Westinghouse had no control whatever in the educational program other than in supplying funds to make it available (R-42a). During the first four years under the program, a participant devoted 32 hours per week on his regular work assignment for Westinghouse and attended classes at either Carnegie Tech or Pitt for the other eight hours as a regularly enrolled student (R-82a). During this period, each respondent was paid his full salary as an engineer at Westinghouse on which income tax was paid (Tr-40).[2]

During the fifth year of the program (after having satisfactorily completed the scholastic requirements of the respective universities to proceed) the participants were granted an educational leave of absence of nine to twelve months from their employment to allow them time to conduct research and to write and defend a thesis topic as required by the universities for the granting of the degree. During this leave, the plaintiffs had no duties and performed no services whatever for Westinghouse (Tr-53), all of their time being devoted to their research and thesis topic.

The nature of the thesis topics selected by the respondents was not in any way related to the work being done at Westinghouse except to the extent that it was in the field of engineering and science (Tr-62, 124, 154). The results of the research were of no direct value to Westinghouse and the government neither contended nor offered proof to the contrary (Tr-54).

While on educational leave, Westinghouse, under the program, gave each of the respondents a monthly allow-

(2) "Tr" refers to transcript of testimony.

ance which was a percentage of his salary with adders for the number of children in the family. Westinghouse also paid the tuition, books, fees, etc.

Previous to the educational leave, each of the respondents was receiving a salary from Westinghouse for services rendered which was commensurate with the salaries of other engineers at Westinghouse. Subsequent to the termination of the educational leave and upon resumption of their employment services with Westinghouse, the respondents again received salaries which were commensurate with the salaries of other engineers employed at Westinghouse (Tr-72).

The trial of the case before a jury in the district court evolved into an issue of law, rather than an issue of fact. Must a scholarship grant to an individual who is a candidate for a degree at an educational institution be in the nature of a gift (that is, must there be an absence of any motive of self-interest on the part of the grantor in making the scholarship grant) in order for the scholarship to be excludable under Section 117 of the Internal Revenue Code.

Upon equivocal instructions by the court in submitting the case to the jury, the jury answered in the negative the interrogatory

> "Were the amounts received by (respondents) from Westinghouse as scholarship at an educational institution excludable from gross income."

In reversing, the court of appeals stated

> "Appellants' stipends were awarded as subsidies to fulltime students, in an amount varying in appropriate relation to each recipient's needs. Their continuance was contingent upon the participants' maintenance of the academic standards required of a candidate for a graduate degree by the university which each appellant

> attended. While receiving these grants, appellants were on an academic leave of absence from their employment for the specific purpose of completing their doctoral dissertations. These are the most important positive characteristics which appellants' grants share with scholarships generically. * * *" (Petitioners' Appendix B, page 7a).

The court of appeals concluded that the grant to the respondents as candidates for a degree at an educational institution was a scholarship within the meaning of Section 117 of the Internal Revenue Code and that the grantor's subjective intention in making the scholarship grant available was irrelevant (Petitioners' Appendix B, page 13a).

Reasons Why the Writ Should Not Be Granted

1. The decision of the third circuit in this case is in conformity with the decision of the Tax Court of the United States, *William Wells,* 40 T. C. 40 (1963) where the Tax Court stated, at page 49:

> "But the language of Section 117 and its legislative history make it clear that amounts received as a scholarship or fellowship grant may be compensatory in character and may still be excludable from income."

and also the decision of the Tax Court in *Clarence Peiss,* 40 T. C. 78, wherein the Court stated, page 82:

> "It is no longer of interest whether transfers that are scholarship or fellowship grants are gifts."

The Commissioner of Internal Revenue has not appealed the decision of *Wells,* has acquiesced in the decision; and moreover, has announced that the applicable regulations will be amended accordingly. Revenue Ruling 65-59, I. R. B. 1965-1.

All that remains to be done to eliminate the asserted conflict which the petitioner relies on and one which he himself has structured and nurtured is for him to fulfill his oft-announced promise to amend the ambiguous and equivocal regulations involved. See *Elmer L. Reese, Jr.*, 45 T. C. 407, footnote 6, page 416.

2. The judgment of the court of appeals is that the judgment of the district court will be reversed and the case remanded for proceedings not inconsistent with the opinion of the court of appeals.

The government's position with respect to the case at this juncture is that the decision of the court of appeals calls for a new trial and not for the entry of judgment for the taxpayers (See footnote 7, page 6, Petition for Writ).

If this contention is proper and the judgment of the court of appeals is not a final decision but only a reversal with directions to grant a new trial, then the Petition for a Writ of Certiorari should be denied as not involving a final decision. *Slaker vs. O'Connor*, 278 U. S. 188, 49 S. Ct. 158.

Conclusion

The Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

DOUGHERTY, LARRIMER, LEE & HICKTON,

By JAMES C. LARRIMER,
Attorneys for Respondents-Taxpayers.

In the Supreme Court of the United States

OCTOBER TERM, 1968

No. 473

JOHN H. BINGLER, DISTRICT DIRECTOR OF INTERNAL REVENUE, PETITIONER

v.

RICHARD E. JOHNSON, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

REPLY BRIEF FOR THE PETITIONER

In their brief in opposition, respondents neither deny that the decision below is in conflict with the decisions of several other circuits nor challenge the administrative need to resolve the resulting uncertainty in the application of the scholarship and fellowship exclusion of Section 117 of the Internal Revenue Code. Instead, asserting "conformity" between the decision below and *Wells* v. *Commissioner*, 40 T.C. 40, they insist that the conflict may be resolved through implementation of the Commissioner's stated intention [1] to amend the Treasury Regulations to conform with *Wells* and similar cases.

[1] See Rev. Rul. 65–59, 1965–1 Cum. Bull. 66.

321-933—68

Wells, however, involved a problem remote from this case. The issue was the taxability of amounts received by a New York University graduate student who, in fulfilling requirements for a Ph.D. degree, participated in a Veterans Administration training program. The student was not a VA employee prior to the training and was not obligated to undertake future employment with it. The Tax Court found as a fact that the primary purpose of the training program was to train students to be clinical psychologists with nothing more than the hope that they might work for the Veterans Administration upon graduating, and any services that the student rendered during the training period were not of substantial value to the Veterans Administration. Such services were (40 T.C. at 48) "under close supervision by staff psychologists" who "could have accomplished the same tasks in little more time than they spent supervising and counseling" the students. Here, in contrast, only Westinghouse employees were eligible for the Bettis program; participation was subject to Westinghouse and AEC approval; the selection of these topics was closely supervised; and respondents and all other participants were obligated to return to work at the Bettis Laboratory of Westinghouse.

The Internal Revenue Service announced some time ago that it was considering amending the Regulations under Section 117 so as to conform the Regulations to the results reached in *Wells* and similar cases. But any such amendment obviously would not cover the situation here or in the cases in the Fourth, Fifth, Sixth, and Tenth Circuits and Court of Claims that have reached results in conflict with the decision below. It has been and continues to be the position of the Internal Revenue Service that amounts paid by an employer to an employee on educational leave with

a commitment thereafter to render services to the employer are not excludable fellowships or scholarships. Neither the Internal Revenue Service's treatment of *Wells* nor the proposed Regulations are inconsistent with this approach.[2] This is evidenced by the position of the Service in the present case. The Internal Revenue Service has expressly advised us that no change in this position, by regulation or otherwise, is contemplated.[3]

Respectfully submitted.

ERWIN N. GRISWOLD,
Solicitor General.

OCTOBER 1968.

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[2] The acquiescence of the Internal Revenue Service in *Evans* v. *Commissioner*, 34 T.C. 720, see 1965–1 Cum. Bull. 4, where the taxpayer was obligated to work for her grantor upon completing her studies or to refund the sums advanced, may be inconsistent with the position above. Compare the decision here (Appendix to the petition, p. 14a & n. 5) with *Stewart* v. *United States*, 363 F. 2d 355, 357 (C.A. 6). Although *Evans* may be distinguished in that the recipient was not and had never been employed by the grantor when she received her stipend, the Internal Revenue Service has advised the Assistant Attorney General in charge of the Tax Division that because the Service is of the view that a grant conditioned on future employment is not a fellowship or scholarship, the *Evans* acquiescence will be modified.

[3] Respondent's argument that the petition should be denied because the judgment of the court of appeals is not a final decision is not well taken. The court of appeals has acted finally on the appeal before it and directed that there be further proceedings in conformity with a changed rule of law. This Court has commonly granted certiorari in such circumstances inasmuch as the ruling "is fundamental to the further conduct of the case." *United States* v. *General Motors Corp.*, 323 U.S. 373, 377; see, also, *Hanover Milling Co.* v. *Metcalf*, 240 U.S. 403, 408; *Donruss Co.* v. *United States*, 384 F. 2d 292 (C.A. 6), certiorari granted, 390 U.S. 1023.

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In the Supreme Court of the United States

OCTOBER TERM, 1968

No. 473

JOHN H. BINGLER, DISTRICT DIRECTOR OF INTERNAL REVENUE, PETITIONER

v.

RICHARD E. JOHNSON, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE PETITIONER

OPINIONS BELOW

The district court's instructions to the jury are not officially reported. They are unofficially reported at 19 A.F.T.R. 2d 426. The opinion of the court of appeals is reported at 396 F. 2d 258.

JURISDICTION

The judgment of the court of appeals was entered on June 5, 1968. The petition for a writ of certiorari was filed on September 3, 1968, and was granted on November 18, 1968. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether amounts, measured by prior salary and family size, paid by Westinghouse Electric Corporation to selected employees to whom Westinghouse had granted an educational leave of absence for the purpose of completing a doctoral dissertation, and who were obligated to continue in Westinghouse's employ for at least two years after the leave, are excludable from the recipient's gross income as a "scholarship" or "fellowship" within the purview of Section 117 of the Internal Revenue Code of 1954.

STATUTE AND REGULATIONS INVOLVED

Section 117 of the Internal Revenue Code of 1954 and the relevant provisions of the Treasury Regulations on Income Tax promulgated thereunder are set forth in the Appendix, *infra*, pp. 37–41.

STATEMENT

Respondents[1] were employees of the Bettis Atomic Power Laboratory in Pittsburgh, Pennsylvania, which Westinghouse Electric Corporation operates under a cost plus contract with the Atomic Energy Commission (R. 71–72, 78; Tr. 256–257, 290). Each respondent participated in the Westinghouse Bettis Fellowship and Doctoral Program, one of a variety of training programs that Westinghouse offers to its employees (R. 7–9, 60; Tr. 30–32, 226). In view of a severe shortage of qualified nuclear scientists and engineers, the Bettis doctoral program was established

[1] Messrs. Johnson, Pomerantz and Wolfe are referred to herein as "respondents". Their wives are parties solely because joint tax returns were filed for the years in question.

in 1956 to recruit and retain engineers and scientists and thereby aid in meeting the needs of Westinghouse for key professional personnel. (R. 42, 58, 76, 81–82; Tr. 154, 155, 219, 277, 300–303). The program is funded primarily by the AEC under its general contract for the operation of the Bettis Laboratory (R. 58,, 64–65, 71, 77; Tr. 220, 236, 256, 287) and is limited to engineers and scientists employed at the Bettis Laboratory who wish to seek a Ph.D. in engineering or science at either the University of Pittsburgh or Carnegie Institute of Technology (R. 9, 37, 61–62, 99; Tr. 33, 124, 227–229, Pl.'s Ex. 2). As of the date of trial in this case, approximately 60 Westinghouse employees had obtained doctorates through the Bettis program. (R. 59; Tr. 222.)

Bettis engineers participating in the program first enter a "work-study" phase, during which they hold a regular job at Westinghouse and attend classes part time[2] either at the University of Pittsburgh or Carnegie Institute of Technology (R. 12–13, 26–27, 44–45, 100–104; Tr. 39, 80, 161; Pl.'s Ex. 2). Those who complete all preliminary requirements for a doctorate—*i.e.*, course work, language studies, and qualification examinations—may apply for an "educational" leave of absence in which to complete a dissertation. Each applicant must be approved by Westinghouse and by the AEC and the topic of his proposed thesis is reviewed to ensure that it is relevant to the work program of the laboratory. (R. 61–62, 74–76; Tr. 228–229, 273–276.) Those selected must agree to work at Bettis for at least two years after completion of their leave. Earlier, when

[2] Westinghouse allows its employees up to eight hours per week (up to 156 hours each year) of paid "release time" in which to attend classes. (R. 102–103; Pl.'s Ex. 2.)

respondent Wolfe took his leave, only a one year commitment was required. (R. 8–9, 21–22, 35–36, 47–48, 62–63, 109, 110; Tr. 32, 33, 63, 116, 119, 168, 230–231; Deft. Exs. 1, 3.)

While on educational leave an engineer receives payments from Westinghouse based on a fixed percentage of his prior salary at Westinghouse plus amounts that depend on the size of his family, up to a fixed maximum. (R. 63, 106; Tr. 231–232; Pl.'s Ex. 2.) Westinghouse's internal records designate those on educational leave of absence as employees of the Bettis Laboratory. The stipends paid are charged to the indirect labor overhead of the laboratory, and Westinghouse treats these amounts as wages for withholding and social security tax purposes. (R. 68–69; Tr. 247–249.) Those on leave retain their seniority status (R. 70; Tr. 253–254) and receive all employee benefits, such as hospitalization, insurance, and stock option privileges (R. 36–37, 48, 63; Tr. 121, 169–170, 232). They continue to contribute to and accumulate rights under the Westinghouse pension plan, and are eligible for vacation immediately upon return from leave. (R. 36–37, 48, 63; Tr. 121, 169–170, 232.)

After successfully completing the work-study phase of the Bettis program, each of the three respondents in this case was granted a leave of absence for the purpose of writing a thesis on topics that Westinghouse and the AEC had approved. During leaves of nine months, respondents Johnson[3] and Pomerantz[4]

[3] Respondent Johnson was on leave from October 1, 1960, to June 30, 1961. (R. 7; Tr. 30.)

[4] Respondent Pomerantz was on leave from November 1, 1961, to July 31, 1962. (R. 8; Tr. 31.)

were each paid $5,670, representing 80 percent of their prior salaries at Westinghouse. Respondent Wolfe, whose leave lasted a year,[5] received $9,698.90, which amounted to 90 percent of his prior salary. (R. 7–8; Tr. 30, 31, 32.)

Westinghouse withheld income tax from these amounts. Respondents filed claims for refund, contending that the payments were excludable from gross income as scholarships under Section 117 of the Internal Revenue Code of 1954. The Commissioner of Internal Revenue rejected these claims, and timely refund suits were brought in the district court.

At a consolidated trial, the court instructed the jury that (R. 90; Tr. 428–429):

> amounts of money or stipends paid to an individual to enable him to pursue studies or research are considered to be amounts received as a scholarships or fellowship grant if the primary purpose of the studies or research is to further the education and training of the recipient in his individual capacity * * *.

The instructions continued, however, to note that a scholarship or fellowship does not include an amount that either represents "compensation for past, present or future employment services, or represents payment for services which are subject to the direction or supervision of the grantor" or are "paid to an individual to enable him to pursue studies or research which studies or research are primarily for the benefit of the grantor * * *." (R. 90; Tr. 429.)

[5] Respondent Wolfe was on leave from March 1, 1960, to February 28, 1961. (R. 8; Tr. 31.)

In answer to special interrogatories, the jury found that the amounts received by each respondent from Westinghouse did not constitute excludable scholarships or fellowship. (R. 89–90, 99; Tr. 428, 449.) Judgment accordingly was entered in favor of the District Director. (R. 111–112; Judgment).

On appeal the Court of Appeals for the Third Circuit reversed, holding that the amounts paid to respondents during their educational leaves of absence were excludable, and that the issue should not have been submitted to the jury.[6] (R. 129; Slip op 11.) The court reasoned that even if a payment had " 'indicia of compensation' ", it could nonetheless be characterized as an excludable scholarship. Accordingly, the court disapproved (R. 124; Slip op 5–6) the provision of Section 1.117–4(c)(1) of the Income Tax Regulations, which states that Section 117 does not encompass amounts that represent "compensation for past, present, or future employment services." It also ruled that the amounts paid respondents were not compensation for future employment at Westinghouse, since respondents, after completing their doctorates, were to be paid at a rate commensurate with their then education and experience. (R. 127; Slip op 9.) Finally, the court held (R. 128; Slip op 10–11) that whatever "indirect advantage" the Bettis program gave Westinghouse was beyond the scope of Section

[6] Because respondents did not move for either a directed verdict or judgment n.o.v. at trial, we interpret the decision below as calling for a new trial and not the entry of judgment for respondents. See *Globe Liquor Co.* v. *San Roman*, 332 U.S. 571; *Cone* v. *West Virginia Paper Co.*, 330 U.S. 212; *Johnson* v. *New York, N.H. & H.R. Co.*, 344 U.S. 48, 54, n. 3.

1.117-4(c)(2) of the Regulations, which states that amounts "paid or allowed to * * * an individual to enable him to pursue studies or research primarily for the benefit of the grantor" are not a "scholarship" or "fellowship".

SUMMARY OF ARGUMENT

The Westinghouse program under which respondents received 80 or 90 percent of their prior salary while completing their doctoral theses is typical of a variety of programs sponsored by private and public employers that allow an employee to complete a graduate degree while continuing to receive all or substantially all of his prior salary. The question here is whether amounts employees receive under such programs fit within the exclusion from gross income of amounts received as a "scholarship" or "fellowship" that Congress created when it enacted Section 117 of the Internal Revenue Code of 1954.

The statute does not provide a general definition of these terms. However, Congress plainly expressed the view that the exclusion would not apply to grants that are "in effect merely payments of a salary during a period while the recipient is on leave from his regular job." H. Rep. No. 1337, 83d Cong., 2d Sess. 17; *accord,* S. Rep. No. 1622, 83d Cong., 2d Sess. 18. To the extent that Congress could foresee such arrangements, it expressly prohibited or limited the tax exemption. Thus Section 117(b)(1) requires that taxable income include amounts students receive in return for teaching, research or other services. Section 117(b)(2) requires that non-degree candidates include in income

grants received to finance research or study, except for those paid by governmental, charitable or other tax exempt organizations, and then the exclusion is limited to $300 per month up to a maximum of three years.

The Treasury has implemented this expression of Congressional purpose in regulations that define the terms "scholarship" and "fellowship". These Regulations provide that, generally speaking, scholarships and fellowships are amounts paid to or for the benefit of an individual, to aid him in study or research. The Regulations, however, then specifically exclude from the meaning of "scholarships" and "fellowships" payments which represent compensation for past, present or future employment services or which are paid primarily for the benefit of the grantor. The definition of the Regulations provided the basis for the instructions given the jury at the trial of this case.

Prior to the decision below, four circuits, the Court of Claims, and the Tax Court agreed that bargained-for payments such as respondents received here are not "scholarships" or "fellowships". The Third Circuit, however, here held invalid the "compensation" test, and construed the alternative "primary purpose" test of the regulation as meaning a test of who benefits the most from the studies or research rather than what is the primary purpose of the grant itself.

Contrary to the apparent view of the Third Circuit, Congress did not enact Section 117 simply to eliminate income tax on payments made to support a per-

son who is studying or performing research. The legislative history shows an intent to exempt only relatively small amounts paid to students who would not otherwise have a substantial tax liability. At the same time Congress made clear its purpose to tax continuing salary payments to people on leave from their regular jobs, as was so plainly the case here.

Respondents' entire arrangement with Westinghouse was bargained for; two of the respondents expressly acknowledged the importance this program played in their decision to accept employment with Westinghouse. They received a doctorate, while supported by Westinghouse, in exchange for a commitment to remain with Westinghouse for two years after completing their study. The arrangement relieved Westinghouse of the need to recruit qualified engineers in a highly competitive market, and respondents gave up their freedom to negotiate for jobs on the open market for a period of two years.

Moreover, the work done by the respondents fit into the over-all research program of the Bettis Laboratory, which was run by Westinghouse and the Atomic Energy Commission. While the opportunity to get a Ph.D. at Westinghouse's expense unquestionably assisted the recipients in the pursuit of their studies, it constituted a very attractive fringe-benefit that induced respondents to accept employment with Westinghouse. The payments to respondents can reasonably be characterized only as compensatory in nature, made primarily to benefit Westinghouse, and the decision below is wrong in allowing these payments to be excluded from the recipients' income. It should be re-

versed here, and the judgment of the district court should be reinstated.

ARGUMENT

INTRODUCTION

The respondents in this case received stipends from their employer, Westinghouse, while on educational leave to complete work on doctoral degrees in engineering. Only selected employees of Westinghouse were eligible for this program. (R. 9, 62; Tr. 33, 229–230.) Respondents retained employee status during their graduate work (R. 36–37, 48, 63, 68–69; Tr. 121, 169–170, 232, 247–249) and, as a condition precedent to receiving the stipends, they specifically obligated themselves to remain with Westinghouse for two years after completion of the Ph.D. programs. (R. 8–9, 21–22, 35–36, 47–48, 62–63, 109, 110; Tr. 32–33, 63, 116, 119, 168, 230–231; Def's. Exhs 1 & 3.) The payments to the respondents while on leave were geared to their regular salary, plus a family allowance. (R. 63, 106; Tr. 231–232; Pl's. Ex. 2.)

Numerous employers provide similar programs for their employees. Not infrequently, as in the case of the federal government,[7] the employee receives his full

[7] See Rev. Rul. 64–71, 1964–1 Cum. Bull. (Part I) 82, which deals with grants by the National Institute of Public Affairs to enable Government employees to attend selected universities for an academic year of study. Although not mentioned in the ruling, the Government Employees Training Act, 5 U.S.C. 4101–4118, requires participants to return to the government for a period three times as long as the leave. See 5 U.S.C. 4108. The Internal Revenue Service allows exclusion from income of amounts the Institute paid to cover tuition, books and classroom expenses. However, the continuing salary payments the recipients received from the department, bureau, or agency where they were employed are includible in income. Here, the

salary while on educational leave. Ordinarily, the recipient promises—generally in a written contract[8]—to work for the employer for a specified period of time after his leave. Thus the employee surrenders his future freedom to bargain and the employer is relieved of the need to recruit a highly trained replacement in a tight labor market.

The issue in this case arises under Section 117 of the Internal Revenue Code of 1954. The text of this provision is set out in full in the Appendix (*infra*, pp. 37–38). Essentially, though, the question involves the proper construction of the words "scholarship" and "fellowship grant," as used in the first paragraph of the section.

As so often happens in such cases, dictionary definitions are not of much help in working out the proper

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amounts Westinghouse applied to respondents' tuition, books, and fees have been treated as not includible in their gross income. Conceptually these sums are properly includible in income, although they may be offset by an educational expense deduction. For a description of the circumstances under which such amounts may be deducted, see, generally, § 1.162–5 of the Income Tax Regulations.

[8] Compare *Mark* v. *Commissioner*, decided November 3, 1967 (26 T.C.M. 1106), involving a foreign service officer employed by the State Department, who was a fellow at the Harvard Center for International Affairs. Although no particular course of studies was required by the State Department, and the taxpayer was not required to return to his employment at the State Department at the end of his fellowship, the State Department continued to pay taxpayer's regular salary during his attendance at the Center, because it believed that the program offered valuable training for the participants and increased their qualifications for positions of higher responsibility. The Tax Court held that the payments to the taxpayer by the State Department while he was a fellow at the Center were not excludable as a fellowship grant.

ambit of these words as used in the statute. It is relevant to note, though, that both "scholarship" and "fellowship" were in origin words used in connection with Universities, and with a charitable connotation. They are not applicable, we submit, to payments made in a commercial setting, or to payments made by an employer to an employee as a part of an employment arrangement.

Neither the statutory language nor the legislative history provide conclusive guides, but it is entirely clear that Congress was of the view that it was not exempting from tax payments that were simply continuations of salary to an employee on educational leave.

This legislative view receives expression in the pertinent Treasury Regulations, which formed the basis for the instructions given the jury at the trial of this case. The Third Circuit stands alone in rejecting this interpretation; four other courts of appeals and the Court of Claims have approved the Treasury's view. We shall now turn to that history and the regulations in order to demonstrate that the amounts Westinghouse paid respondents during their leaves are exactly the type of receipts that Congress intended should not be exempted from income tax.

I. CONGRESS DID NOT INTEND THAT SECTION 117 WOULD ALLOW EXCLUSION FROM INCOME OF AMOUNTS REPRESENTING CONTINUING SALARY PAYMENTS OR WHICH ARE OTHERWISE COMPENSATORY IN NATURE

Many grants denominated "scholarships" or "fellowships" create no taxable income to the recipient because they go from grantor to recipient with no

quid pro quo required. The source might be a school, an eleemosynary organization, or an individual; but the essential characteristic is that the recipient is only a student and is not expected to provide consideration for his grant beyond continuing his studies and, perhaps, maintaining a specified level of academic achievement. The grantor might act from any one of a variety of motives; his purpose might be entirely charitable or result from an interest in the welfare of a particular student. In no event, however, would he expect or receive any benefit other than the satisfaction of providing a student with an opportunity that he otherwise might not have had. The Internal Revenue Code of 1939 and its predecessor Revenue Acts provided an acceptable method of determining the tax consequences of such payments to the recipients, for such amounts qualified for the exclusion from income taxation that these laws conferred upon "gifts". See, *e.g.*, Section 22(b)(3) of the Internal Revenue Code of 1939; Section 22(b)(3) of the Revenue Act of 1928, 45 Stat. 797; Section 213(b)(3) of the Revenue Act of 1918, 40 Stat. 1065.

This approach proved unsatisfactory, however, when the Treasury, in the later 1940's, sought to deal with two other types of grants. These, while used for the support of students or researchers, differed importantly from what has traditionally been considered a "scholarship" or "fellowship". One was the foundation grant paid to a post-doctoral researcher.[9] In this

[9] See I.T. 4056, 1951-2 Cum. Bull. 8; *Stone* v. *Commissioner*, 23 T.C. 254.

instance the recipient is, in all essence, being paid to do his life's work; yet, strictly speaking, he is not receiving "salary" or "compensation" because he has no obligation to the grantor, and the grantor does not exercise day to day control over his work. If the first factor controlled, the grant would be "income"; if the second, it might be a "gift".

Comparable difficulties arose in the treatment of amounts paid research or teaching assistants, *i.e.*, graduate students who received grants and in return were expected to conduct research or teach classes.[10] Plainly the recipients were chosen only because of their student status and the payments were designed to support them while completing their education; in these respects the payments resembled fellowships. On the other hand, the recipients were employees of and required to perform services for the grantors, an obvious hallmark of taxable income.

The Commissioner of Internal Revenue had no means of resolving these difficulties except through application of the provisions that exclude "gifts" from income. Thus he ruled (I.T. 4056, 1951–2 Cum. Bull. 8, 10):

> The amount of a grant or fellowship award is includible in gross income unless it can be established that such amount is a gift. If a grant or fellowship award is made for the training and education of an individual, either as a part of his program in acquiring a degree or in otherwise furthering his educational development, no services being rendered as consideration there-

[10] See *Banks* v. *Commissioner*, 17 T.C. 1386; *Ti Li Loo* v. *Commissioner*, 22 T.C. 220.

> for, the amount of the grant or award is a gift which is excludable from gross income. However, when the recipient of a grant or fellowship applies his skill and training to advance research, creative work, or some other project or activity, the essential elements of a gift as contemplated by Section 22(b)(3) of the Internal Revenue Code are not present, and the amount of the grant or fellowship is includible in the recipient's gross income.

This approach ran into difficulty in the Tax Court. That tribunal agreed with the Commissioner in the case of research assistants, and held their grants to be taxable income. *Ti Li Loo* v. *Commissioner,* 22 T.C. 220; *Banks* v. *Commissioner,* 17 T.C. 1386. On the other hand, foundation grants to established researchers were ruled to be nontaxable. *Stone* v. *Commissioner,* 23 T.C. 254.

These results were defensible if the problem were viewed simply as one of interpreting the word "gift". But in terms of basic tax policy, the outcome was anomalous. The graduate student receiving a subsistance income—Mr. Banks' monthly stipend varied from $175 to $237.50 between mid-1947 and early 1949—was taxed because he was unquestionably an employee being paid to perform services in return for his grant. Yet the beneficiary of the foundation grant who continued his ordinary professional activities, and was paid an amount commensurate with his professional status—Mr. Stone received $3,000 from a foundation while on sabbatical from a university which continued half his regular salary for the 1950–1951

academic year—escaped taxation because the grantor proceeded from a "disinterested generosity".

To alleviate the difficulties of a rule that required a case-by-case inquiry into the question whether a "gift" was intended, Congress wrote Section 117 into the Internal Revenue Code of 1954 (H. Rep. No. 1337, 83d Cong., 2d Sess. 16; S. Rep. No. 1622, 83d Cong., 2d Sess. 17). Section 117(a) states that "gross income does not include * * * any amount received * * * as a scholarship * * * or * * * as a fellowship grant * * *." Although there is no general statutory definition of the words "scholarship" and "fellowship", the Ways and Means Committee said (H. Rep. No. 1337, *supra,* at 17, "Such grants generally are of small amount and are usually received by individuals who would have little or no tax liability in any case."

Then, special provisions were written to cover the two problems that had proved so vexing to the Treasury. Thus section 117(b)(1) specifically provides that the "scholarship" exclusion does not apply to payments made for teaching, research, or other services in the nature of part-time employment required as a condition to receiving the grant. Then, in a provision obivously directed at situations such as that in *Stone* v. *Commissioner, supra,* Section 117(b)(2) provides that non-degree candidates may exclude grants only if they are paid by governmental agencies or charitable, educational and other tax-exempt "organizations described in Section 501(c)(3)," and then only in the amount of $300 for each month of the grant's duration, for a maximum of 36 months.

In speaking of Section 117(b)(2) the Ways and

Means Committee described its purpose in these words (*Id.* 17):

> This will tax those grants which are in effect merely payments of a salary during a period while the recipient is on leave from his regular job. Hence, in the case of persons who have completed their formal education and are continuing to teach or carry on research as part of their life work, the grant will be excluded only if it is merely a supplement to the individual's own funds which make it possible for him to carry on research or further his educational development.

The Senate rejected the House formulation of Section 117(b)(2),[11] which would have allowed exclusion only of grants that, together with compensation received from the recipient's prior employer, did not exceed 75 percent of his prior year's salary. See H. Rep. No. 1337, *supra,* at p. 17. It wrote the language that is now in Section 117(b)(2), expressing, however, the same purpose as the House (S. Rep. No. 1622, *supra* at p. 18):

> The House bill provided a specific standard for determining the taxability of grants received by individuals who are not candidates

[11] The House draft of Section 117(b)(2) was criticized on the grounds that the test discriminated against post-doctoral students, such as physicians taking advanced training in a specialty who had received no significant prior salary, and because it would increase costs to non-profit foundations which sponsored such training. See, *e.g.*, statement of Mefford R. Runyon, Executive Vice President, American Cancer Society, Hearings Before the Senate Committee on Finance, April 14, 1954, at pp. 921–924; Letter from Detlev W. Bronk to Senator Milliken, dated April 16, 1954, *id.* at pp. 1367–1368.

> for a degree, typically the recipients of post doctoral fellowships. Such grants may be in effect a continuing salary payment while the recipient is on leave from his regular job. The House bill specified that such grants are excludible only if the annual amount of the grant plus any compensation received from the recipient's previous employer is less than 75 percent of the recipient's salary in the year preceding the grant. Cases were brought to your committee's attention in which the formula of the House bill would tax grants which were clearly not a continuing salary payment. In many of these cases taxability would result from the absence of a substantial earned income in the previous year. Your committee therefore has substituted for the 75 percent rule an exclusion of $300 per month of grants paid to individuals who are not candidates for degrees. The exclusion will not be allowed beyond a total of 36 months.

See, also, *id.* at 188–190.

The thrust of the legislation and its history is clear: Generally speaking, amounts paid for the support of a scholar constitute an excludable scholarship or fellowship. On the other hand, payments are not excludable simply because their purpose is to pay the living expenses of a person who is a student, for amounts that relate to the provision of services or some other *quid pro quo* by the recipient must be included in gross income as they are in the same category as the "continuing salary payments" that Congress repeatedly said should not be exempted.

II. THE PERTINENT TREASURY REGULATIONS UNDER SECTION 117 PROPERLY IMPLEMENT THE CONGRESSIONAL PURPOSE OF DENYING THE EXCLUSION TO CONTINUING SALARY PAYMENTS AND OTHER COMPENSATORY ARRANGEMENTS

Because the statute contains no general definition of "scholarship" and "fellowship", the Treasury has sought to fill the void through its power to "prescribe all needful rules and regulations for the enforcement" of the Internal Revenue Code, 26 U.S.C. 7805(a). As this Court recently held (*United States* v. *Correll*, 389 U.S. 299, 306–307):

> * * * We do not sit as a committee of revision to perfect the administration of the tax laws. Congress has delegated to the Commissioner, not to the courts, the task of prescribing "all needful rules and regulations for the enforcement" of the Internal Revenue Code. 26 U.S.C. § 7805(a). In this area of limitless factual variations, "it is the province of Congress and the Commissioner, not the courts, to make the appropriate adjustments." *Commissioner* v. *Stidger*, 386 U.S. 287, 296.

The regulations under Section 117, which four circuits and the Court of Claims have sustained, are plainly reasonable "contemporaneous constructions by those charged with administration of these statutes which should not be overruled except for weighty reasons." *Commissioner* v. *South Texas Co.*, 333 U.S. 496, 501.

Scholarships and fellowships are, of course, amounts paid to support a student or scholar while he is pursuing studies or independent research, and this is the

position taken in the relevant Treasury Regulations. Thus Section 1.117–3(a) and (c) of the Income Tax Regulations provide (Appendix, infra, pp. 39–40): "A scholarship generally means an amount paid or allowed to, or for the benefit of, a student, whether an undergraduate or a graduate, to aid such individual in pursuing his studies." On the other hand, it is equally clear that a payment is not a "scholarship" or "fellowship" merely because it is used to support an individual engaged in study or research. Payments which result from a bargained-for transaction or are a *quid* given for the recipient's *quo* do not fit the common understanding of those words.[12] At the very least, as the court of appeals recognized in the present case (R. 127; Slip Op 9.):

> A significant commitment by the student in return for a grant would, of course, place that grant outside the category "scholarship", at least to the extent of the value of that commitment. For if the grantee had to barter for his stipend, giving full value for it, this arrangement would hardly serve the primary purpose of the Section 117 exclusion: to encourage financial aid to education through tax relief.

[12] Thus, see National Industrial Conference Board Publication No. 209, Combating Knowledge Obsolescence: I. Company Fellowship Plans (1968). This report analyzes (*id.*, ii) 75 "fellowship" plans sponsored by 60 corporations. Under those plans "no student is ever *required* to agree to employment as a condition of receiving a fellowship", even though most of the grantors hope to recruit the recipients of their funds (*id.*, 6). The only string attached to any of these grants has to do with patentable inventions developed by the recipient during his graduate study. Some, but comparatively few, of the grantors reserve title or a royalty free license to such inventions; most, however, do not (*id.*, 59–60).

As we have shown above, Congress is in obvious agreement with this view, for to the extent that it foresaw such compensatory arrangements, it expressly forbade or limited the tax exemption in Section 117 (b). In a similar vein the applicable Treasury Regulations, following the general definition of "scholarship" and "fellowship", provide (Section 1.117–4(c)) (Appendix, *infra*, pp. 40–41):

> § 1.117–4 *Items not considered as scholarships or fellowship grants.*
>
> (c) *Amounts paid as compensation for services or primarily for the benefit of the grantor.* (1) Except as provided in paragraph (a) of § 1.117–2 [not relevant here] any amount paid or allowed to, or on behalf of, an individual to enable him to pursue studies or research, if such amount represents either compensation for past, present, or future employment services or represents payment for services which are subject to the direction or supervision of the grantor.
>
> (2) Any amount paid or allowed to, or on behalf of, an individual to enable him to pursue studies or research primarily for the benefit of the grantor.
>
> * * * * *

Thus, under the first paragraph of the regulation, amounts that represent compensation for past, present or future employment—*i.e.*, paid from the employer to an employee—are not considered a scholarship or fellowship. This is a simple and direct implementation of the Congressional expression that exemption should not be allowed to continuing salary payments to an

employee who is on leave from his regular job. To this the Treasury added a second provision, holding that a scholarship or fellowship does not include amounts that finance study or research undertaken "primarily for the benefit of the grantor". By this paragraph, the Treasury has supplemented the first in order to impose tax on bargained-for arrangements that do not create an employer-employee relation, as, for example, in the case of an independent contractor. But the general idea is the same: "scholarship" or "fellowship" does not include arrangements where the recipient receives money and in return provides a *quid pro quo*.

III. THIS COURT SHOULD FOLLOW THE DECISIONS OF FOUR CIRCUITS AND THE COURT OF CLAIMS ACCEPTING THE FORMULATION OF THE TREASURY REGULATIONS WHICH FORMED THE BASIS FOR THE INSTRUCTIONS GIVEN THE JURY HERE

In this jury case, the rule of law applied at trial was that expressed in the instructions given the jury, and those (see p. 5 *supra;* R. 86–96; Tr. 420–441) were in substance the same as the regulations. Under that definition of "scholarship" and "fellowship", Westinghouse's payments to respondents must fail to qualify for exclusion from taxation. The opportunity to obtain a doctorate while supported by Westinghouse was a valuable fringe benefit that strongly influences an engineer to enter into Westinghouse's employ (R. 22, 34–35; Tr. 66, 113, 115–116.)

Working for Westinghouse during the work-study phase was the first requirement of the later, paid leaves of absence. (R. 104; Pl's. Exh. 2.) Westinghouse would not have paid the so-called "stipends"

but for respondents' commitments to work for one or two additional years (R. 62–63; Tr. 230–231), and their choice of theses topics that fit into the overall research program of the Bettis Laboratory. (R. 61–62, 74–75; Tr. 228–229, 273–275.) The payments were simply continuing salary payments to employees who were granted leave so that they might upgrade skills required by Westinghouse, requirements that Westinghouse otherwise could not have so readily fulfilled. (R. 42, 58, 76, 81–82; Tr. 154–155, 219, 277, 300–303.) As two of the respondents testified, the availability of the Bettis program was a strong inducement in their decisions to accept employment at Westinghouse.[18] Westinghouse avoided the need to recruit new people, and respondents increased their skills and attractiveness to Westinghouse, and surrendered their freedom of choice of employers for a significant period of time.

Under the instructions, the jury, we submit, had no choice but to find for the government on this record; at the very least the record has an adequate base for the jury verdict if the Treasury's Regulations on which the instructions were based are a valid interpretation of the words "scholarship" and "fellowship."

1. Four courts of appeals and the Court of Claims have sustained the Regulations that the Third Circuit

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[18] Mr. Pomerantz testified that in interviewing with Westinghouse, he was interested not only in a job but in a job which would allow him to continue his education. (R. 22; Tr. 66.) Mr. Johnson testified that of the items he considered in accepting the job with Westinghouse, the doctoral program was most important, the salary second, and the fringe benefits last. (R. 35; Tr. 115.)

refused, to apply here. The first case was *Ussery* v. *United States*, 296 F. 2d 582, where the Fifth Circuit held that Section 117 did not allow a taxpayer to exclude from gross income monthly stipends he received from the Mississippi Department of Public Welfare, which had granted him educational leave while he secured his Master's Degree in social work. While on leave the employee was given the benefit of all automatic salary adjustments, accrued annual and sick leave, retirement benefits, and workmen's compensation. He was bound to return to the department after completing his studies. In sustaining Section 1.117–4 (c)(2) of the Regulations as a reasonable interpretation of the statute, the court reasoned (296 F. 2d at 586):

> There is nothing in the legislative history to indicate that the statute was designed to exclude from gross income all payments made to enable individuals to participate in a program of educational value. It is a fair inference that the terms "scholarship" and "fellowship" were used as opposed to a term such as "compensation" and were carefully selected to bar cases where a payment is made for work primarily for the benefit of the grantor. We conclude that the Regulation excluding such payments from the reach of Section 117 is sound and proper.

The court held that the payments in question fell within the barred category, because the purpose of the program was to train employees so that they could benefit the Department of Welfare by performing their duties more effectively.

In *Stewart* v. *United States*, 363 F. 2d 355, the

Sixth Circuit considered the case of a taxpayer who received an educational leave and grant from her employer, the Tennessee Department of Public Welfare, to pursue a master's degree in social work. The Sixth Circuit ruled (*id.*, 357) that the payments she received were includible in gross income because the factors present, *i.e.*, her contractual obligation to return to the employ of the department upon completion of the leave, and her retention of Civil Service status, retirement and other fringe benefits, were such "indicia of 'compensation for past, present or future services'" as to be excluded from the definition of "scholarship" and "fellowship" under the Regulation. Even though no services were performed for the grantor during the leave of absence, the evidence of a continuing employment relationship between the grantor and recipient was so strong that the court concluded (*ibid.*) "that here the stipend was compensation for past and future services."

In like manner, the Court of Claims decided in *Reiffen* v. *United States*, 376 F. 2d 883, that gross income must include amounts paid to an employee of M.I.T.'s Lincoln Laboratory who was assigned no work responsibility during an eight month period while he was a full time graduate student, completing research and other requirements for a Ph. D. in electrical engineering. Because the primary purpose of the program was to enable Lincoln to compete with industry and other organizations in the recruitment and retention of scientific and professional personnel, the court, resting on and approving Regulation Section 1.117–4(c), held that Lincoln's payments were made to

enable the engineer to pursue studies and research primarily for the benefit of Lincoln.

In *Reese* v. *Commissioner*, 373 F. 2d 742, the Fourth Circuit affirmed, *per curiam*, a Tax Court decision, 45 T.C. 407, that payments received by a student-teacher from the County Board of Education for one semester of teaching, which was a degree requirement, did not constitute an excludable scholarship because such payments were in fact compensation for services rendered. In *Woddail* v. *Commissioner*, 321 F. 2d 721 (C.A. 10), the Veterans Administration had supported a resident in psychiatry and neurology who obligated himself to remain an employee of the Veterans Administration for a specified time in return for each year of resident training. The Tenth Circuit held that the amounts paid to the taxpayer must be included in his gross income because (321 F. 2d at 724) "it was an amount paid for services and was primarily for the benefit of the grantor." Decisions of the Tax Court and various district courts are in accord.[14]

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[14] See also *Bonn* v. *Commissioner*, 34 T.C. 64; *Littman* v. *Commissioner*, 42 T.C. 503; *Zolnay* v. *Commissioner*, 49 T.C. 389; *DiBona* v. *Commissioner*, decided September 24, 1968 (27 T.C.M. 1055); *Kopecky* v. *Commissioner*, decided September 24, 1968 (27 T.C.M. 1061); *Mark* v. *Commissioner*, decided November 3, 1967 (26 T.C.M. 1106); *Lingl* v. *Charles* (S.D. Ohio), decided December 15, 1967 (21 A.F.T.R. 2d 419). Compare *Pappas* v. *United States* (E.D. Ark.), decided March 27, 1967 (67-1 U.S.T.C., par. 9386); *Spruch* v. *Commissioner*, decided March 6, 1961 (20 T.C.M. 324); *Wrobleski* v. *Bingler*, 161 F. Supp. 991 (W.D. Pa.); *Bhalla* v. *Commissioner*, 35 T.C. 13; *Wells* v. *Commissioner*, 40 T.C. 40; and *Peiss* v. *Commissioner*, 40 T.C. 78, where the respective courts upheld the regula-

2. The Third Circuit stands virtually alone in its approach to the problem.[15] It said of Section 1.117–4(c)(1) of the Regulation, which denies the exclusion to "compensation for past, present, or future employment services" (R. 124; Slip Op 5–6):

> In light of the aim explicit in the legislative history of doing away with the touchstone of

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tion, but found as a matter of fact that the primary purpose of the payments in those cases was to further the education and training of the recipient.

[15] *Evans* v. *Commissioner*, 35 T.C. 720, acquiescence 1965–1 Cum. Bull. 4, where the taxpayer was obligated to work for her grantor upon completing her studies or to refund the sums advanced, may be consistent with the Third Circuit's position. Although *Evans* may be distinguished in that the recipient was not and had never been employed by the grantor when she received her stipend (see Rev. Rul. 65–146, 1965–1 Cum. Bull. 66), the Internal Revenue Service has advised the Assistant Attorney General in charge of the Tax Division that because the Service is of the view that a grant conditioned on future employment is not a fellowship or scholarship, the *Evans* acquiescence will be modified.

See, also, *Broniwitz* v. *Commissioner*, decided September 30, 1968 (27 T.C.M. 1088), which held that stipends paid to a degree candidate, a full-time student directing his own course of study, not obligated to work for the grantor after receiving his degree, were excludable under Section 117, even though he was required to work for the grantor during the summer when he was nominally carried on the grantor's rolls as an employee. Although the Tax Court judge cited *Johnson* v. *Bingler* with approval, he concluded (*id.*, 1092):

> In the instant case the fact situation is much stronger than it was in *Bingler*, *supra*. Petitioner was not an employee of Raytheon in any meaningful sense prior to receiving the fellowship. * * * Neither was petitioner obligated in any way to perform any services for Raytheon upon graduation. * * *; in fact, he went to work for North American Aviation shortly after he was awarded his doctorate.

> compensation versus gift, we cannot say, as one court has, that "indicia of compensation" such as are suggested by the regulation are legitimate criteria for testing the excludability of an alleged scholarship, *cf. Stewart* v. *United States*, 363 F. 2d 355, 357 (6th Cir. 1966). Nor can we even approve the disqualification added by Treas. Reg. §1.117–4(c)(1) (1956) of amounts which represent "compensation for past, present, or future employment services," without more. *Contra, Ussery* v. *United States*, 296 F. 2d 582, 586–87 (5th Cir. 1961). This ruling seems merely an attempt to write into the regulations a concept which was considered and intentionally rejected by the Congress which enacted the Code.

This analysis, however, is directly refuted by the legislative history. Although Congress did seek a solution more appropriate than a determination of whether a "gift" was intended, it did not intend to avoid an inquiry into whether a particular arrangement represented compensation for services; indeed both the House and Senate Committees show exactly the contrary. Far from reading into the regulations a "concept which was considered and intentionally rejected by the Congress", Regulation Section 1.117–4(c)(1) finds its direct antecedent in Congress' own expressions of its purposes.

The record here is conclusive in its showing of the type of situation that Congress intended not to exempt from taxation. From the beginning there was a continuing employment relationship between Westinghouse and respondents. Participation in the doctoral program was restricted to regular employees of Westinghouse. (R. 9, 62, 99; Tr. 33, 229; Pl's. Ex. 2.) Prior

to their "leaves of absence", taxpayers worked at Westinghouse under a "work-study" arrangement, whereby they were allowed "release time" from their jobs to attend classes required for their degrees. (R. 104; Pl's. Ex. 2.) Thereafter, they were required to remain with Westinghouse.

Westinghouse's internal records designated those individuals on educational leaves of absence as employees of the Bettis Laboratory. (R. 68–69; Tr. 247–249.) They continued to participate in the company health insurance, life insurance, pension plans and employee stock option plans. (R. 36–37, 48, 63; Tr. 121, 169–170, 232). Retirement benefits, seniority benefits and vacation benefits continued to accrue without interruption during the leave. (R. 36–37, 48, 63; Tr. 121, 169–170, 232.) The stipends paid during the leave were based on a fixed percentage of the recipient's prior salary, plus a family allowance, up to a fixed maximum. (R. 63; Tr. 231–232.) They were substantial in amount, representing either 80 or 90 per cent of the recipient's prior salary. (R. 7–8, 106; Tr. 30–32; Pl's. Ex. 2.) The payments were charged to the indirect labor overhead of the laboratory (R. 68–69; Tr. 247–249), and Westinghouse treated those amounts as wages for withholding and social security purposes. (R. 68–69; Tr. 247–249.) The AEC contract with Westinghouse had no provisions for offering scholarships or fellowships, but while on leave respondents were paid under this contract as employees, with the AEC refunding most of the payments to Westinghouse. (R. 68, 77; Tr. 248, 287–288.)

Each was obligated to return to Westinghouse's employ. (R. 8–9, 21–22, 35–36, 47–48, 62–63, 109, 110;

Tr. 32–33, 63, 116, 119, 230–231, Def's. Exs. 1 & 3.) Thus the amounts were "continuing salary payments to an employee on leave from his regular job"—just what Congress said should not be considered a tax exempt "scholarship" or "fellowship" (H. Rep. No. 1337, *supra*, at p. 17; S. Rep. No. 1622, *supra*, p. 18). The amounts paid to respondents are not the relatively small sums given to people who would not be expected to pay much tax, another characteristic Congress ascribed to the "scholarships" and "fellowships" to which it was granting exemption. (H. Rep. No. 1337, *supra*, at p. 17). Indeed, if the decision of the Third Circuit is sustained, the many people in respondents' position will receive exactly the windfall allowed to the taxpayer in *Stone* v. *Commissioner*, *supra*, under the 1939 Code, even though Congress thought it had, in Section 117(b)(2), limited such freedom from tax to people receiving relatively small stipends, from government or charitable organizations, before they entered upon their life's work.

The court below itself recognized that (R. 127; Slip Op. 9) "A significant commitment by the student in return for a grant would, of course, place that grant outside the category of a 'scholarship', at least to the extent of the value of that commitment." But it is not necessary, as that court thought (R. 127; Slip Op. 9), for the recipient to agree to work for less than a "'commensurate' salary" after completing his degree or to enter into a specifically enforceable contract. Freedom to bargain was surrendered; at the least, respondents for two years lost their chance to

bargain for a salary better than Westinghouse's average. And if any of them failed to live up to his promise to return to Westinghouse, he would be liable for the latter's out-of-pocket costs. For, the party agrieved by breach of an agreement at least "is entitled to be reimbursed for the money actually paid out and for all reasonable and proper expenses incurred on the faith of the contract." *Harman* v. *Chambers,* 358 Pa. 516, 521–522, 57 A. 2d 842, 845; see, also, *Kerns* v. *Insurance Co.,* 11 Pa. Superior Ct. 209; *Jessup & Moore Paper Co.* v. *Bryant Paper Co.,* 129 Atl. 559; *Emerman* v. *Baldwin,* 186 Pa. Superior Ct. 561, 142 A. 2d 440.

3. As for the part of the regulation that denies the exclusion to amounts "paid * * * an individual to enable him to pursue studies or research primarily for the benefit of the grantor", the court below, quoting its prior decision in *Commissioner* v. *Ide,* 335 F. 2d 852, 855, thought it necessary to "observe and emphasize that under this regulation [§ 1.117–4(c)(2)] the determinative consideration is not the primary purpose of the grantor in subsidizing the student, but rather the primary purpose of and the primary benefit from the subsidized study." The problem inherent in this interpretation is that the studies and research pursued always benefit the student-grantee whose training or education is thereby advanced, but they directly benefit the grantor only in the case where the grantor is also interested in the thesis or other objective results of those studies and research. The Third Circuit's approach would never impose tax where the grantor will benefit only in the future, as Westing-

house did here.[16] Yet in such circumstances the payment is unquestionably part of a *quid pro quo* exchange for an obligation or services that come after or before the recipient's studies or research. Where a payment is essentially compensatory or part of a *quid pro quo* exchange, it is irrelevant that the grantor derives no immediate, direct benefit from the subsidized study. When, as here, the grantor-employer receives an agreement to give future services, he receives something of considerable consequences in the uncertain labor markets in which he does business.

Moreover, the Third Circuit's inquiry, which might be phrased "Who benefits from the study or research the most", is administratively impracticable. It requires a separate evaluation of the benefits to the grantor and those to the recipient and then, in some manner, a comparison of each. Such an exercise would be a meaningless juxtaposition of factors that are not necessarily related to one another or to the Congressional purposes.

The Commissioner's test, on the other hand, requires an examination of the program as a whole, and asks one question: what was the primary function of the support given under the particular program. And the exclusion is denied only where the answer is that the grant was made because the recipient provided the grantee with a significant and valuable consideration.

On this side of the case, the record plainly war-

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[16] This is almost always the case where the grantor is also the employer of the grantee and will always benefit by the further education and training of his employee.

ranted a verdict for the government. The opportunity to obtain a doctorate while employed at Westinghouse was part of the over-all package of salary and fringe benefits for which respondents bargained when they first entered into corporate employment. The purpose of the program then was to attract competent people, to keep them, and to make certain that they continued to work for Westinghouse after receiving a doctorate. In all of its attributes the program was designed with the thought of alleviating Westinghouse's difficulties in hiring engineers in the open market. In working for Westinghouse before their doctoral leaves, and in agreeing to return to Westinghouse thereafter, each of the respondents thus conferred a valuable benefit on Westinghouse by reducing its need to go out in the market and hunt for new people.

Moreover, the thesis work done during respondent's leave also conferred a benefit to Westinghouse, which was concededly an important factor in the structure of the Bettis program. Both Westinghouse and the Atomic Energy Commission exercised specific controls to insure the general relevance of the proposed thesis topics to the work program at Bettis. (R. 74–75; Tr. 273–274.) Significantly, conduct of this research was the only purpose of the "leave," since all other requirements of the doctorate had to be met beforehand. Some topics submitted were disapproved and subsequently withdrawn. (R. 62, 75; Tr. 229, 276.) Mr. M. Daugherty of the AEC testified (R. 75; Tr. 274–275):

> One of the specific reasons for doing this was that the Atomic Energy Commission has always

> believed that a man should have a job relatedness in his training assignments. * * *
> * * * if a man is to be trained in a specialty, then that specialty should be related to his field of interest and his work assignment or future work assignment.

The specific topics chosen by respondents were "job related"[17] and Westinghouse felt free to treat the work product as its own.[18]

Thus the benefits to Westinghouse were substantial. Of course respondents also benefited. But that was not the primary objective. The Bettis Doctoral program obviously would not have existed but for Westinghouse's needs, and its judgment, shared by the AEC, that those needs would be met through this program.

4. The correct view of the decision below was expressed in *Quasi* v. *United States* (D. Minn.), decided November 21, 1968 (22 A.F.T.R. 2d 5850), where the district court explicitly refused to follow the Third Circuit's decision: In *Quast* the taxpayer was a doctor who embarked upon a master's program in physica' medicine and rehabilitation at the University of Minnesota Medical School while he was on the staff of the Minneapolis Veterans Administration

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[17] Mr. Pomerantz testified that he worked in the heat transfer and fluid flow section of Westinghouse and that his thesis topic was the effect of increased gravity on film boiling—a problem concerning heat transfer and fluid flow. (R. 11, 15–16; Tr. 37, 46.) Mr. Johnson testified that while at Westinghouse he specialized as a mechanical metallurgist, and that his thesis topic was in the field of mechanical metallurgy. (R. 29–30; Tr. 95.)

[18] Mr. Johnson testified that his thesis was published as a Bettis document. (R. 34; Tr. 111.)

Hospital. He agreed to work for the Veterans Administration for a period of 24 months after completion of his residency, and received some $5,000 from the Veterans Administration during the first six months of 1964, while he was a full time student at the medical school and performed no services for the Veterans Administration. The Government's contention that this sum was simply salary was sustained, and the taxpayer's challenge to the validity of Treasury Regulations Section 1.117–4(c) rejected, with the court ruling (22 A.F.T.R. 2d 5859):

> To follow the view of *Johnson* would permit nearly any payment labeled "scholarship" or "fellowship" and not expressly within the restrictions of Sec. 117(b)(1) to be excluded from gross income. The court does not believe that the legislative history of this section leads to that conclusion.

Exemptions from tax are of course to be strictly construed.[18] Congress itself pointed to the way in which the exemption of Section 117 is to be restricted. That way is reasonably and correctly expressed in the Treasury Regulations.

The Bettis Doctoral Program represented an attractive fringe benefit to the employee and an assured source of scientific and professional personnel to Westinghouse. Respondents received most of their salary while on "leave" and the purpose of the leave was to allow them to engage in research on a subject of interest to Westinghouse and the AEC. In return,

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[18] *E.g.*, *Commissioner* v. *Jacobson*, 336 U.S. 28; *Helvering* v. *Northwest Steel Mills*, 311 U.S. 46.

respondents surrendered for a significant time their freedom to solicit job offers in a highly competitive market. Congress never intended that the terms "scholarship" and "fellowship" would connote such a *quid pro quo* arrangement as the one manifested here. The jury instructions were correct, the evidence supported—indeed compelled—the verdict, and the court of appeals should have sustained the result.

CONCLUSION

The decision below should be reversed and the judgment of the district court should be reinstated.

Respectfully submitted.

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JANUARY 1969.

APPENDIX

Internal Revenue Code of 1954:

SEC. 117. SCHOLARSHIPS AND FELLOWSHIP GRANTS.

(a) *General Rule.*—In the case of an individual, gross income does not include—

(1) any amount received—

(A) as a scholarship at an educational institution (as defined in section 151(e)(4)), or

(B) as a fellowship grant,

including the value of contributed services and accommodations; and

(2) any amount received to cover expenses for—

(A) travel,

(B) research,

(C) clerical help, or

(D) equipment,

which are incident to such a scholarship or to a fellowship grant, but only to the extent that the amount is so expended by the recipient.

(b) *Limitations.*—

(1) *Individuals who are candidates for degrees.*—In the case of an individual who is a candidate for a degree at an educational institution (as defined in section 151(e)(4)), subsection (a) shall not apply to that portion of any amount received which represents payment for teaching, research, or other services in the nature of part-time employment required as a condition to receiving the scholarship or the fellowship grant. If teaching, research, or other services are required of all candidates (whether or not recipients of scholarships or fellowship grants) for a particular degree as a condition

to receiving such degree, such teaching, research, or other services shall not be regarded as part-time employment within the meaning of this paragraph.

(2) *Individuals who are not candidates for degrees.*—In the case of an individual who is not a candidate for a degree at an educational institution (as defined in section 151(e)(4)), subsection (a) shall apply only if the condition in subparagraph (A) is satisfied and then only within the limitations provided in subparagraph (B).

(A) *Conditions for exclusion.*—The grantor of the scholarship or fellowship grant is an organization described in section 501(c)(3) which is exempt from tax under section 501(a), the United States, or an instrumentality or agency thereof, or a State, a Territory, or a possession of the United States, or any political subdivision thereof, or the District of Columbia.

(B) *Extent of exclusion.*—The amount of the scholarship or fellowship grant excluded under subsection (a)(1) in any taxable year shall be limited to an amount equal to $300 times the number of months for which the recipient received amounts under the scholarship or fellowship grant during such taxable year, except that no exclusion shall be allowed under subsection (a) after the recipient has been entitled to exclude under this section for a period of 36 months (whether or not consecutive) amounts received as a scholarship or fellowship grant while not a candidate for a degree at an educational institution (as defined in section 151(e)(4)).

(26 U.S.C. 1964 ed., Sec. 117.)

Treasury Regulations on Income Tax (1954 Code):

§ 1.117-1 *Exclusion of amounts received as a scholarship or fellowship grant.*

(a) *In general.* Any amount received by an individual as a scholarship at an educational

institution or as a fellowship grant, including the value of contributed services and accommodations, shall be excluded from the gross income of the recipient, subject to the limitations set forth in section 117(b) and § 1.117–2. The exclusion from gross income of an amount which is a scholarship or fellowship grant is controlled solely by section 117. Accordingly, to the extent that a scholarship or a fellowship grant exceeds the limitations of section 117(b) and § 1.117–2, it is includible in the gross income of the recipient notwithstanding the provisions of section 102 relating to exclusion from gross income of gifts, or section 74(b) relating to exclusion from gross income of certain prizes and awards. For definitions, see § 1.117–3.

* * * * *

(26 C.F.R., Sec. 1.117–1.)

§ 1.117–3 *Definitions.*

(a) *Scholarship.* A scholarship generally means an amount paid or allowed to, or for the benefit of, a student, whether an undergraduate or a graduate, to aid such individual in pursuing his studies. The term includes the value of contributed services and accommodations (see paragraph (d) of this section) and the amount of tuition, matriculation, and other fees which are furnished or remitted to a student to aid him in pursuing his studies. The term also includes any amount received in the nature of a family allowance as a part of a scholarship. However, the term does not include any amount provided by an individual to aid a relative, friend, or other individual in pursuing his studies where the grantor is motivated by family or philanthropic considerations. If an educational institution maintains or participates in a plan whereby the tuition of a child of a faculty member of such institution is remitted by any other participating educational institution attended by such child, the amount

of the tuition so remitted shall be considered to be an amount received as a scholarship.

* * * * * *

(c) *Fellowship grant.* A fellowship grant generally means an amount paid or allowed to, or for the benefit of, an individual to aid him in the pursuit of study or research. The term includes the value of contributed services and accommodations (see paragraph (d) of this section) and the amount of tuition, matriculation, and other fees which are furnished or remitted to an individual to aid him in the pursuit of study or research. The term also includes any amount received in the nature of a family allowance as a part of a fellowship grant. However, the term does not include any amount provided by an individual to aid a relative, friend, or other individual in the pursuit of study or research where the grantor is motivated by family or philanthropic considerations.

* * * * * *

(26 C.F.R., Sec. 1.117–3.)

§1.117–4 *Items not considered as scholarships or fellowship grants.*

* * * * * *

(a) *Educational and training allowances to veterans.* * * *

(b) *Allowances to members of the Armed Forces of the United States.* * * *

(c) *Amounts paid as compensation for services or primarily for the benefit of the grantor.* (1) Except as provided in paragraph (a) of § 1.117–2, any amount paid or allowed to, or on behalf of, an individual to enable him to pursue studies or research, if such amount represents either compensation for past, present, or future employment services or represents payment for services which are subject to the direction or supervision of the grantor.

(2) Any amount paid or allowed to, or on behalf of, an individual to enable him to pursue

studies or research primarily for the benefit of the grantor.

However, amounts paid or allowed to, or on behalf of, an individual to enable him to pursue studies or research are considered to be amounts received as a scholarship or fellowship grant for the purpose of section 117 if the primary purpose of the studies or research is to further the education and training of the recipient in his individual capacity and the amount provided by the grantor for such purpose does not represent compensation or payment for the services described in subparagraph (1) of this paragraph. Neither the fact that the recipient is required to furnish reports of his progress to the grantor, nor the fact that the results of his studies or research may be of some incidental benefit to the grantor shall, of itself, be considered to destroy the essential character of such amount as a scholarship or fellowship grant.

(26 C.F.R., Sec. 1.117–4.)

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SUPREME COURT, U. S.

FEB 13 1969

No. 473

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1968

JOHN H. BINGLER,
District Director of Internal Revenue,
Petitioner

v.

RICHARD E. JOHNSON, *et al.*

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE RESPONDENTS

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Petitioner

v.

RICHARD E. JOHNSON, *et al.*

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE RESPONDENTS

QUESTION PRESENTED

Whether an employer may make a scholarship grant to an employee (who is a degree candidate at an educational institution) which may be excludible from gross income under Section 117 of the Internal Revenue Code of 1954 without the necessity of establishing such grant as a gift.

STATEMENT

This is an income tax case. At issue is what is a scholarship excludible under Section 117 of the Code. More specifically, the issue is "Does a scholarship lose its tax-exempt status under Section 117 if (1) the grantor of the scholarship has a motive of self-interest in making it available, or

(2) there is any indicia of compensation surrounding the grant of the scholarship." The Third Circuit says "No"; the Fifth and Sixth Circuits say "Yes".

Respondents were employees of Westinghouse Electric Corporation at its Bettis Atomic Power Laboratory. Each had a degree from an accredited college in engineering. (Tr. 35, 76, 158, App. 10, 25, 43)

Westinghouse had initiated a doctoral program which provided employees of the company with the opportunity of securing the degree of Doctor of Philosophy in Engineering and Science at either the University of Pittsburgh or Carnegie Institute of Technology (now Carnegie-Mellon University). (Plaintiffs' Exhibit 2, App. 99, Tr. 33, App. 9) The existing requirements of the respective universities for the granting of the degree were not changed. (Tr. 136, 183, App. 40, 51)

During the first four years under the program, the respondents devoted 32 hours per week on their regular work assignments for Westinghouse and attended classes at either Carnegie Tech or Pitt for the other eight hours as regularly enrolled students. (Plaintiffs' Exhibit 2, App. 99, Tr. 40, 80, 161, App. 13, 26, 44) During this period, each respondent was paid his full salary as an engineer at Westinghouse on which income tax was paid and which is not in issue. (Tr. 40, 161, App. 13, 45)

During the fifth year (having satisfactorily completed the scholastic requirements of the respective universities to proceed) each respondent was granted an educational leave of absence of nine to twelve months from his employment (Tr. 30, 31, App. 7, 8) to allow him time to conduct research and to write and defend a thesis topic (Plaintiffs' Exhibit 2) as required by the universities for the granting of the degree. During this leave period, the respondents had no duties and performed no services for Westinghouse, all of their time being devoted to their research and thesis topic at the respective universities. (Tr. 53, 101, 164, App. 18, 32, 46)

As part of the doctoral program, Westinghouse gave each of the respondents "an educational stipend" during the leave period which was a percentage of his monthly salary based on his marital status and size of family with a maximum limitation as follows (Plaintiffs' Exhibit 2, App. 106):

Marital Status	Percent of Salary	Maximum
Single	70%	$490.00
Married	80%	$560.00
Married with one child	85%	$595.00
Married with two or more children	90%	$630.00

Westinghouse also paid the cost of tuition, books, fees, etc.[1] Before going on educational leave, each respondent agreed that he would return to Westinghouse at the end of the leave period and remain in the employ of Westinghouse for at least two years[2] thereafter at a salary commensurate with the duties assigned. (Tr. 32, 33; App. 8, 9)

The requirements of the respective universities for the granting of the degree of Doctor of Philosophy required that the particular thesis topic to be researched and defended qualify as original research. (Tr. 137, 187, App. 40, 52) The selection of a particular topic was a matter of collaboration between the student and his faculty advisor (Tr. 138, 185, App. 40, 51) because the faculty advisor had to be satisfied that the topic had not theretofore been researched and would meet the approval of the university as original research for the granting of the degree. (Tr. 139, 187, App. 40, 52) After selection of the thesis topic and approval by the university, the topic was submitted to Westinghouse and the Atomic Energy Commission for approval. (Tr. 48, 128, App. 17, 38)

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[1]Income tax was withheld from the educational stipends but not from the payments made for tuition, books, fees, etc. (Tr. 313, App. 84)

[2]Wolfe was not asked to sign an agreement but was informed that he was expected to return to his employment for a period at least equivalent to his leave period. (Tr. 33, App. 9)

Each of the respondents selected, researched, wrote and defended such a thesis after which the written article became a part of the library of the respective university and available to the public generally. (Tr. 52, 111, 144, App. 18, 34) The research results were of no direct value to Westinghouse and the government neither contended nor offered proof to the contrary.[3]

During the entire doctoral program, respondents were enrolled as students at the respective universities in the same manner (Tr. 38, 80, 160, App. 12, 26, 44) and were required to meet the same scholastic standards for the degree as other graduate students. (Tr. 142, App. 41) Westinghouse had no control of the educational program other than in supplying funds to make it available. (Plaintiffs' Exhibit 2, App. 99, Tr. 136, 154, App. 40, 42)

Claims for refund of the tax withheld from the educational stipends were filed with and rejected by the Internal Revenue Service and suit was filed.

The trial of the case before a jury in the District Court evolved into an issue of law, rather than an issue of fact, the government contending that Westinghouse had a motive of self-interest in making the scholarship available by using it to attract engineering personnel to its employ and that such motive precluded tax exemption for the scholarship; the respondents contending that evidence of such self-interest and of compensation generally was irrelevant in determining a scholarship under Section 117.

After admitting evidence in support of both contentions, the trial court then instructed the jury on the respective contentions of the parties (Tr. 428, 431, 432, App. 89, 90,

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[3]Significantly, respondent Johnson had selected and researched a thesis topic during his leave period in 1961 which he abandoned before completion because of the lack of time and equipment. (Tr. 98, App. 31) He selected another thesis topic which he successfully pursued after termination of the leave period and for which he was granted the degree of Doctor of Philosophy in 1965. (Tr. 103, App. 33) Westinghouse did not continue the original 1961 research project abandoned by Johnson. (Tr. 316, App. 85)

91) and allowed the jury to select the applicable law with an equivocal interrogatory:

> "Were the amounts received by [respondents] from Westinghouse a scholarship at an educational institution excludible from gross income?" (Tr. 428, App. 89)

which was answered in the negative by the jury.

The Court of Appeals for the Third Circuit reversed, stating that the issue should not have been submitted to the jury and that

> "In the light of the aim explicit in the legislative history of doing away with the touchstone of compensation vs. gift, we cannot say, as one Court has, that 'indicia of compensation' such as are suggested by the regulation are legitimate criteria for testing the excludibility of an alleged scholarship. . . . Nor can we even approve the disqualification . . . of amounts which represent 'compensation for past, present, or future employment services' without more. . . . This ruling seems merely an attempt to write into the regulations a concept which was considered and intentionally rejected by the Congress which enacted the Code. (Slip Op., App. 124)
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> "In the light of this overriding congressional goal of encouraging scholarship aid and the accompanying lack of restrictions as to its amount or character in the case of degree candidates, we believe, upon due consideration, the appellants' educational grants do qualify for income tax purposes as excludible scholarships or fellowship grants." (Slip Op., App. 129)

The government sought certiorari because the decision of the Third Circuit is in conflict with the decisions of *Ussery v. United States,* 296 F.2d 582 (C.A. 5) and *Stewart v. United States,* 363 F.2d 355 (C.A. 6) which disqualify the tax free status of a scholarship to a student who is a candidate for a degree at an educational institution where there is any "indicia of compensation" or where the educational stipend may be considered "compensation for past, present, or future employment services."

SUMMARY OF ARGUMENT

The government's argument is that a scholarship or fellowship grant which has "indicia of compensation" attached to it or which may be considered generically "compensation for services" is disqualified from tax-exempt status as a scholarship or fellowship under Section 117.

The taxpayers' argument is that Congress did not intend that the determination of a scholarship or fellowship grant be made by a reference to general considerations of "gross income" or "compensation for services".

Congress recognized that a scholarship or fellowship grant is gross income and compensation for services. However, it did not intend that such grants should be taxable but that they should be treated as tax-exempt within the limits provided in the Code.

Congress recognized that there is no middle ground between a gift and compensation in the format of the Internal Revenue Code in which a scholarship or fellowship may qualify exclusively. Admittedly, an educational grant is not a gift. Undeniably, it is compensation; and because it is, Congress did not intend that a scholarship or fellowship grant under Section 117 and an educational grant with indicia of compensation be mutually exclusive by definition. They can be and are one and the same.

So long as the amount paid is to enable the individual to pursue his education, it is (1) a scholarship if he is a student and a degree candidate at an educational institution, and (2) a fellowship if he is not a degree candidate but the grantor meets the qualifications of Section 117(b).

In other words, the comparison test of "gift *vs.* compensation" has been replaced by the curriculum standards of the educational institution in respect of scholarships and the tax-exempt status of the grantor and the amount and time limitation in respect of fellowships.

The provisions of Section 117 were intended by Congress as a means of limiting compensation in the form of a schol-

arship or fellowship grant entitled to tax-exempt status. Congress did not intend that a scholarship or fellowship grant must be completely free of "indicia of compensation" before it acquires tax-exempt status under Section 117.

ARGUMENT

A. CONGRESS DID NOT INTEND THAT A SCHOLARSHIP UNDER SECTION 117 BE DETERMINED BY REFERENCE TO GENERAL CONSIDERATIONS OF COMPENSATION

The 1939 Internal Revenue Code did not treat scholarships and fellowships specifically and such grants were includible in gross income unless the elements of a gift could be established. The House Committee, in formulating Section 117 of the 1954 Code, attempted to eliminate "the existing confusion as to whether such payments are to be treated as income or as gifts". (H. Rep. No. 1337, 83d Cong., 2d Sess.) By Section 117, Congress sought to provide a "clearcut method of distinguishing between taxable and nontaxable grants" and to eliminate the necessity of deciding the tax status of these grants on a "case by case method". (H. Rep., supra)

A scholarship or fellowship grant is significantly different from a gift in that the latter (in addition to the proper motive) is an executed event while the former is an executory undertaking to use the grant for the recipient's education.

Implicitly, a scholarship or fellowship grant includes a promise to use the funds to further the education of the recipient and/or a condition that the payments shall terminate if they are not so used. Unless it is required that the amounts received be used to further the educational pursuits of the taxpayer, it cannot be said that they are amounts received as a scholarship or fellowship for purposes of Section 117. Revenue Ruling 65-58. With this promise or condition attached to a scholarship or fellowship grant, the payment does not qualify as a gift but is gross income. *Robertson v. United States*, 343 U.S. 711.

Because most grants originate with a corporate or governmental entity which has a motive or purpose in making the educational grant available, *Commissioner v. Ide*, 335 F.2d 852 (C.A. 3), it is unlikely that a grant can qualify as a gift made "out of affection, respect, admiration, charity or like impulses", *Robertson*, supra; or from a "detached and disinterested generosity", *Commissioner v. LoBue*, 351 U.S. 243, 246; or that the payment "proceeded primarily from generosity or charity, rather than from the incentive of anticipated economic benefit", *United States v. Kaiser*, 363 U.S. 299. Undoubtedly, educational grants are made by a grantor with "the incentive of anticipated benefit", *Bogardus v. Commissioner*, 302 U.S. 34, 41, precluding its tax status as a gift.

Therefore, a scholarship or fellowship grant is clearly "gross income" within the liberal definition given to this term by the courts "in recognition of the intention of Congress to tax all gains except those specifically exempted". *Commissioner v. Glenshaw Glass Company*, 348 U.S. 426, 430.

In the context of an employment relationship, any economic or financial benefit conferred on an employee, whatever the form or motive by which it is effected, is included within the term "gross income". And this benefit constitutes "compensation for personal services". *Commissioner v. LoBue*, supra, notwithstanding that the donor derived no economic benefit from it, *Robertson*, supra, or that the payment was entirely voluntary, *Old Colony Trust Company v. Commissioner*, 279 U.S. 716, 730. Therefore, a scholarship or fellowship grant to an employee constitutes compensation for services.

Recognizing that a scholarship or fellowship grant constitutes gross income, Congress provided for exceptions to the general definition of gross income under the 1954 Code:

> "Section 61 (1954 Code) GROSS INCOME DEFINED.
> (a) General Definition—Except as otherwise provided in this subtitle, gross income means all income from whatever source derived . . ."

In commenting on the necessity for this provision in Section 61, the House Report states

> ". . . In view of the fact that certain types of income are excluded from gross income by other sections of the income tax subtitle of the new Code, Section 61(a) contains a clause excepting such income from the general definition of gross income."

Thus, the legislative history indicates that Congress intended that a scholarship or fellowship grant should not be determined by reference to gross income in the generic sense under Section 61. If it is a scholarship under Section 117, it is excludible from gross income even though it may generally constitute gross income under Section 61. By referring to the general concept of gross income or compensation for services in determining what is a scholarship, the whole purpose of Section 117 in providing a specific test is destroyed.

Because a scholarship or fellowship grant requires conduct on the part of the recipient, i.e., to undertake studies or research, such conduct on the part of the recipient is the "quid pro quo" for the grant. The grant then falls within the term "gross income" and can be labelled "compensation for services".

In addition, because a grantor has a purpose to be served in making the grant available, and the acceptance of the grant by the recipient helps fulfill that purpose, there is an "indicia of compensation" which attaches because the grantor benefits from the studies and research undertaken by the recipient under the grant.

Thus, "indicia of compensation" can be found in some form in every scholarship and fellowship grant; and using such comparison as a test to disqualify scholarships and fellowships from tax-exempt status under Section 117, as urged by the government and supported by *Ussery v. United States*, supra, and *Stewart v. United States*, supra, nullifies Section 117.

If the government's view is adopted, every educational grant would be taxable excepting only those grants which are favorably determined administratively on a case by case basis by the Treasury Department. A taxpayer's recourse to a court which follows *Ussery* and *Stewart* as to scholarships and *Duberstein* v. *United States*, 363 U.S. 278, as to gifts, would be fruitless.

It is clear that Congress considered the compensatory aspect of a grant "when the scholarships and fellowships are granted subject to the performance of teaching or research services", (H. Rep., supra) and specifically with respect to those individuals who are not candidates for a degree at an educational institution where the grants ". . . are in effect merely payments of a salary during a period while the recipient is on leave from his regular job." (H. Rep., supra) Congress also considered "research or teaching services in the nature of part-time employment required as a condition to receiving the scholarship or fellowship grant." (H. Rep., supra)

Congress realized that any economic or financial benefit conferred on an employee is "compensation for personal services". *Commissioner v. LoBue*, supra, and considered scholarships and fellowships in the light of "part-time employment" and "continuing salary payments". Had it so intended, Congress could have eliminated the tax exempt status of a scholarship or fellowship grant from an employer to an employee. The Congress, not having done so, the United States Court of Appeals for the Third Circuit is eminently correct in concluding that "indicia of compensation" as a test for the excludibility of a scholarship is "a concept which was considered and intentionally rejected by Congress . . ."

B. CONGRESS DID INTEND TO PROVIDE SEPARATE AND DISTINCT METHODS OF DETERMINING SCHOLARSHIPS AND FELLOWSHIPS EXCLUDIBLE UNDER SECTION 117.

The format of the Section 117 indicates a distinction between scholarships and fellowships excludible under Section 117. Excludible are (1) scholarships at an educational institution and (2) fellowship grants. No further definition of "scholarship" or "fellowship" is given in the statute but the terminology in the limitations in Section 117(b) relating to those who are candidates for a degree and those who are not candidates for a degree indicate that a scholarship refers to an individual who is a candidate for a degree at an educational institution and a fellowship as referring to an individual who is not a candidate for a degree whether or not at an educational institution.

An educational institution is defined in the Code (Section 151(e)(4)) as "only an educational institution which normally maintains a regular faculty and curriculum and normally has a regularly organized body of students in attendance at the place where its educational activities are carried on." The attendance of a student at an educational institution as a candidate for a degree is limited. He either satisfies the curriculum requirements for the degree and is graduated or he fails and/or drops out.

In making specific limitations as between those who are candidates for a degree and those who are not candidates for a degree, Congress must have concluded that in the case of a scholarship where the individual was a candidate for a degree at an educational institution, the requirements of the educational institution for the granting of that degree are a sufficient limitation and guideline to prevent the use of the scholarship grant as a substitute for a salary continuation beyond a reasonable period of time as measured by the time required to secure a degree.

With respect to a fellowship where the individual is not a candidate for a degree, recognizing that a research project

or program of study under a fellowship may have an indefinite duration, Congress placed the limitation of exclusion of 36 months at $300.00 per month with the further requirement that the grantor be government or a tax-exempt organization as defined.

In addition, the legislative history indicates Congress considered scholarships and fellowships separately.

The House report states that Section 117 "excludes from tax all grants to students at educational institutions. . ." and "in the case of individuals who are not candidates for degrees, the bill provides a specific standard to be used in determining whether the grant is in effect a salary payment". Throughout the legislative history, there is a clear distinction between and consideration of those who are candidates for a degree at an educational institution and those who are not candidates for a degree.

Moreover, the regulations promulgated by the Treasury Department in defining a "scholarship" and "fellowship" recognize a distinction between a scholarship and fellowship grant.

> "Regulation Section 1.117-3 Definitions. (a) Scholarship. A scholarship generally means an amount paid or allowed to, or for the benefit of, a *student*, whether an undergraduate or a graduate, to aid such individual in pursuing his studies. . . ."
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> "(c) Fellowship grant. A fellowship grant generally means an amount paid or allowed to, or for the benefit of, an *individual* to aid him in the pursuit of study or research. . . ."

A scholarship requires that the individual be a student at an educational institution and a candidate for a degree in which the student must meet the curriculum requirements of the educational institution for the granting of the degree. On the other hand, a fellowship does not require student status on the part of the individual, nor does it have curriculum requirements of an educational institution as a guideline.

The thrust of the respondents' argument is that scholarships and fellowships were separately considered and treated by Congress because Congress wished to place a limit on the amount of compensation in the nature of a scholarship and fellowship which may be excludible from gross income. Because of the differences between a scholarship and a fellowship as defined, separate limitations had to be provided with respect to each classification.

C. THE EDUCATIONAL STIPENDS RECEIVED BY THE RESPONDENTS QUALIFY AS SCHOLARSHIPS EXCLUDIBLE UNDER SECTION 117.

During his educational leave period, each respondent was a regularly enrolled student as a candidate for a degree at an educational institution which required for the granting of that degree that a research project be undertaken and a thesis written and defended. Living allowances were paid to the respondents to enable them to pursue this research. Therefore the definition of a scholarship under the regulations has been satisfied.

There is no issue as to benefit derived from the research undertaken. Westinghouse derived none directly. It did not request or require that a research project be undertaken by the respondents nor did it specify the particular topic to be researched. (Tr. 47, 84, App. 16, 28)

The government's argument that the living allowances paid to the respondents during their educational leave represent compensation for past, present or future employment services, or represent payment for services which are subject to the direction or supervision of the grantor is without merit.

Unless the term "compensation for past, present, or future employment services" is used in the generic sense of "gross income", this regulation (Section 1.117-4(c)) is inapplicable because each respondent was paid by Westinghouse at the going rate as an engineer for his services previous to

the educational leave. Each was also paid at the going rate as an enginer for his services subsequent to the educational leave, and during his educational leave, he rendered no services to or for the benefit of or subject to the direction or supervision of Westinghouse.

The government is using the term "compensation for services" in the sense that anything paid by an employer to an employee represents compensation for past, present or future services and, therefore, is taxable. This argument is a reversion to the generic sense of "gross income" and overrides the introductory clause of Section 61 of the Internal Revenue Code providing that gross income shall not include items specifically excepted under other sections of the Code. The argument of the government is plainly a reversion to the gift *vs.* compensation test.

The evidence offered by the government during the trial and now adverted to in its argument, of income tax withheld from the stipend, consideration of the respondents as employees during the educational leave period, the manner in which the stipends were recorded on the books of Westinghouse, etc., all establish the fact that there was an employer-employee relationship between Westinghouse and the respondents.

Congress did not intend to disqualify the tax-exempt status of a scholarship or fellowship grant from an employer to an employee. Had it so intended, it could have so provided specifically in the statute. Therefore, evidence tending to establish an employment relationship between the grantor and the recipient of an educational grant is irrelevant in determining the issue involved.

D. THE DECISIONS IN SUPPORT OF THE GOVERNMENT'S CONTENTION FRUSTRATE CONGRESSIONAL PURPOSE IN ENACTING SECTION 117 AND SHOULD NOT BE FOLLOWED.

The express purpose of Congress in enacting Section 117 was to eliminate the existing confusion as to whether scholarships or fellowships are to be treated as income or as gifts and to provide a clearcut method for such determination rather than a case by case method.

As Judge Tannenwald noted in *Elmer L. Reese, Jr.*, 45 T.C. 407, 412,

> "In the light of the decisions. . ., it is questionable whether Congress wholly succeeded in providing greater certainty in this area."

We suggest that this situation has arisen not so much from the statutory provisions but rather from a lack of clarity in the regulations in describing items not considered as scholarships or fellowship grants (Reg. Sec. 1.117-4). Regulations should be explicit and clear up uncertainty rather than create uncertainty. By disqualifying a scholarship if such amount represents either compensation for past, present or future employment services or represents payments for services which are subject to the direction or supervision of the grantor, without a further definition of "compensation for services", any employment relationship renders the scholarship taxable. *Commissioner v. LoBue*, supra. It is this general concept of "compensation" which has resulted in the decisions of *Ussery*, *Stewart* and *Reiffen*.

To disqualify the tax-exempt status of a scholarship if it is compensatory in the generic sense is a reversion to the "gift *vs.* income" test sought to be obviated by Congress. The phrase "compensation for services" as used in the regulation then becomes merely a misnomer for "gross income".

In *Ussery*, the taxpayer was a candidate for a degree at an educational institution with a scholarship furnished him by his employer. As in the present case, there was no issue

of uncompensated past or future services nor were there any services rendered during the educational leave. The degree sought was in the field of social work in which the taxpayer was then employed. In disqualifying the scholarship under Section 117 from tax-exempt status the court noted that

> "The terms 'scholarship' and 'fellowship' connote a purpose of assistance that stands in distinction to the self-interest of an employer in the compensation of his employee.
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> * * * * *
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> "It is a fair inference that the terms 'scholarship' and 'fellowship' were used as opposed to a term such as 'compensation' and were carefully selected to bar cases where a payment is made for work primarily for the benefit of the grantor."

By requiring that the grantor of a scholarship have no motive of self-interest in making the grant available, necessarily the scholarship grantor must be motivated by a charitable or donative intent. And by considering "scholarship" as opposed to "compensation", the court, by misnomer, reverts to the gift *vs.* income test. *Ussery* is badly reasoned and should not be followed.

Similarly, *Stewart* follows *Ussery* and disqualifies the tax-exempt status of a scholarship to a student who was a candidate for a degree at an educational institution. The grantor of the scholarship was her employer and there was no issue that the taxpayer had rendered uncompensated services theretofore or thereafter for which the scholarship represented compensation. The recognition by her employer of her continued status as an employee during the educational leave period was held to be "such indicia of compensation for past, present, or future services as to make the scholarship stipends taxable". Without so stating, the court read further limitations into Section 117 by concluding that where an employment relationship, past or future, is involved between the grantor and the student, the educational grant

cannot qualify as a scholarship but represents taxable compensation for services.

The Court of Claims, as a trial court, in *Reiffen v. United States,* 376 F.2d 883, disqualified a scholarship to a student who was a degree candidate at Massachusetts Institute of Technology because his employer had given him the scholarship as part of a program in recruiting, training and retaining personnel. The court followed *Ussery* and *Stewart.*

However, compare *Reiffen* with *Lawrence E. Broniwitz,* 27 T.C.M. 1088 (decided September 30, 1968), in which the Tax Court held tax-exempt a scholarship to a student who was also a candidate for a degree at Massachusetts Institute of Technology. As in *Reiffen,* the scholarship had been given Broniwitz by his employer as part of his employer's recruiting program. After considering the "indicia of compensation" test of *Ussery* and *Stewart* and the rejection of such test by the United States Court of Appeals for the Third Circuit in this case, the Tax Court stated:

> "We believe that the approach of the Third Circuit in *Bingler* is the correct one, . . ."

The decision in *Reese v. Commissioner,* 373 F.2d 742, affirming the Tax Court, 45 T.C. 407, is not in conflict with the decision in this case. The taxpayer was a candidate for a degree at an educational institution in its teaching program. To secure the degree, she was required to engage in "internship teaching". In fulfilling this requirement, the taxpayer taught at a secondary school for which she received a salary from the school in accordance with the salary scale for other teachers at that school. The court held the amounts taxable, not because they had "indicia of compensation", but because the amount paid was not a scholarship, *i.e.*, it was not paid for the purpose of affording the taxpayer the opportunity to further her education. Rather, the amount was paid for the services actually rendered by the taxpayer as a teacher.

Woddail v. Commissioner, 321 F.2d 721 (C.A. 10), cited by the government as being in conflict with the present case is inapposite. Woddail was not a degree candidate at an educational institution and he actually rendered services which were of direct benefit to his grantor. The issue was whether the amount paid him was a fellowship under Section 117, not a scholarship at an educational institution.

CONCLUSION

It is submitted that this Court's adoption of the government's contention and the test of "indicia of compensation" in determining the excludibility of a scholarship or fellowship grant will continue the pre-1954 Code method of determining the tax status of a scholarship or fellowship grant on a case by case method, contrary to Congressional intention.

For over five years, the Internal Revenue Service has contemplated a revision of the regulations under Section 117. See *Revenue Ruling 65-146*, 1965-1 C.B.; *Revenue Ruling 65-59*, 1965-1 C.B. 67; *Revenue Ruling 63-250*, 1963-2 C.B. 79. Notwithstanding these expressed intentions, no clarification of the regulations has been published. Perhaps this is because there can be no clarification of the regulations in such a manner which would obviate the necessity of a case by case determination of what is a "scholarship *vs.* compensation". A comparison test necessarily requires a case by case determination in the same manner as the test of "gift *vs.* income". See *Duberstein*, supra. Furthermore, there can be no clarification in the description of what is a scholarship which would isolate it from the concept of "compensation for services" and yet not require it to meet the test of a "gift".

For these reasons, the conclusions of the United States Court of Appeals for the Third Circuit in this case should be sustained. This will provide a clearcut method of determining scholarships and fellowship grants as intended by Congress.

Respectfully submitted,

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In the Supreme Court of the United States

OCTOBER TERM, 1968

No. 473

JOHN H. BINGLER, DISTRICT DIRECTOR OF INTERNAL REVENUE, PETITIONER

v.

RICHARD E. JOHNSON, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

REPLY BRIEF FOR PETITIONER

1. The essential thesis of respondents' case is that all monies paid for the support of a degree candidate constitute a "scholarship" and therefore should be excludable from income under Section 117 of the Internal Revenue Code of 1954 unless expressly includible under Section 117(b)(1). (See Br. 11–14.) Yet no authority—indeed not even the Third Circuit in this case—has accepted this interpretation of the statute. Thus the opinion below states (R. 127):

> A significant commitment by the student in return for a grant would, of course, place that grant outside the category "scholarship", at least to the extent of the value of that commitment. * * *

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Respondents, in attempting to distinguish *Reese* v. *Commissioner*, 373 F. 2d 742 (C.A. 4), affirming *per curiam* 45 T. C. 407, and *Woddail* v. *Commissioner*, 321 F. 2d 721 (C.A. 10), make an equivalent concession. In asserting that those decisions are not in conflict with the Third Circuit's here, and are not pertinent to the instant problem, they argue that (Br. 17) "the amount paid [Miss Reese] was not a scholarship * * *. Rather, the amount was paid for the *services actually rendered* by the taxpayer as a teacher" (emphasis supplied). And *Woddail* is distinguished on the ground that the taxpayer (Br. 18) "was not a degree candidate at an educational institution and *actually rendered services* that were of direct benefit to his grantor" (emphasis supplied).[1] Thus, in speaking of services "actually ren-

[1] Respondents' contentions regarding congressional intent (Br. 11–13) are premised on the claim (Br. 11) that the word "scholarship" refers to a grant to a degree candidate while "fellowship" refers to a grant "to an individual who is not a candidate for a degree * * *." The common understanding, however, is different. To the extent that there is a distinction between the terms, the phrase "scholarship" describes grants to an undergraduate student while the word "fellowship" refers only to grants to a graduate student. The bulletin of the Massachusetts Institute of Technology (July 1968) states (p. 82): "A fellowship * * * is a grant to a graduate student which covers his tuition and provides, in addition, a stipend to help defray his living expenses. In the context of the Graduate School, a scholarship is a grant which only covers, or helps to defray, tuition only." It is the general understanding of grantors that the word "fellowship" describes grants to graduate students seeking a degree. See, *e.g.*, National Industrial Conference Board Publication, No. 209, Combating Knowledge Obsolescence: I. Company Fellowship Plans (1968) p. 3; Johns Hopkins Graduate Programs 1968 and 1969, p. 206; Stanford University Bulletin, Series 19, No. 1 (Jan. 2, 1968) p. 54; Graduate School Bulletin of Yale University, Series 63, No. 14, (15 July 1967) pp. 20–21.

dered," respondents mean that there is no scholarship or fellowship if services are performed at the same time as funds are received.

Respondents never explain why Miss Reese's and Dr. Woddail's grants are taxable income but theirs are excludable scholarships. That the former two provided present services, and respondents promised future services as a condition of their grants from Westinghouse, is not a valid distinction. It has long been established that, for purposes of income taxation, it matters not that money is paid in return for services past or services to be rendered in the future. The result must be the same as when services are rendered at the same time as the compensation is received. Nothing in the statute or in the legislative history would exempt respondents' grants as scholarships, while taxing Miss Reese's and Dr. Woddail's as salary.

If the Third Circuit's approach is appropriate, then how is it to be determined whether a commitment is "significant" enough to fall beyond the meaning of the words "scholarship" and "fellowship"? The Third Circuit said that this would occur (R. 127) "if the grantee had to barter for his stipend, giving full value for it * * *." But when would there be a "barter" if not here? If respondents did not give full enough "value" in their promises to return to the Bettis Laboratory for one or two years after completing their doctoral dissertations, when would value be adequate? There are, we suggest, no better measures of a grantee's commitment and its value than this record shows. The Bettis doctoral program was

intended to induce people to come to work for Westinghouse; as two of the respondents expressly conceded, that is exactly what happened (R. 22, 35). The AEC, Westinghouse, and the respondents each considered the promises to return to Bettis for a minimum time an adequate consideration for the grants. Westinghouse needed trains engineers and scientists, and this was an effective way to get them, as the facts of this case show.

Surely, it cannot be said as a matter of law that respondents' commitments were not "significant" enough or that they failed to barter for a full enough "value". At the very least, the significance and value of their commitments and of the paid leave Westinghouse and the AEC allowed them was a matter for the finder of fact to decide.

2. Respondents' argument also misconceives the legislative history. Of course, it is true that Congress wanted to do away with a need to determine on a case by case basis whether a gift was intended. But nothing Congress said sustains respondents' assertion (Br. 10) that Congress therefore intended no inquiry into the existence of salary or other compensation. The legislative history is exactly the converse. As we have pointed out in our opening brief (at pp. 16–18), Congress wrote Section 117(h) with the express purpose of taxing grants "which are in effect merely payments of a salary during a period while the recipient is on leave from his regular job" (H. Rep. No.

1337, 88d Cong., 2d Sess. 17). There could be no more precise characterization of respondents' situation.[2]

The fact that Section 117(b) expressly deals with only two situations—compensation to part-time teaching or research assistants and the government or foundation grant to a non-degree candidate—does not mean that all other grants are exempted under Section 117(a). Respondents concede as much by their treatment of *Reese* and *Wooddail*. The correct view is that Congress in Section 117(b) dealt with the two particular problems that had arisen prior to 1954 and had proved troublesome to the Treasury. As in so many other instances in the administration of the Internal Revenue laws, the then unforeseen problems were to be resolved through the Treasury's authority (26 U.S.C. 7805(a)) "to prescribe all needful rules and regulations for the enforcement" of the Internal Revenue Code.

The regulations under Section 117, which formed the basis for the instructions given the jury here,

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[2] In addition, Congress said (H. Rep. No. 1337, *supra*, 17) of the amounts being exempted in Section 117(a), "[s]uch grants generally are of small amount and are usually received by individuals who would have little or no tax liability in any case." The grants Westinghouse provided respondents do not fit this description. Respondents Johnson and Peramtz each received $5,670 over nine months, representing an annual rate of about $7,300. Respondent Wolfe received $9,698 over a full year. The grants were received at various times between October 1, 1960 and July 31, 1962. (R. 7-8.) Statistics show that during the three years 1960 through 1962 over 70% of individual income tax returns reported adjusted gross income of less than $7,000 and at least 84% reported an adjusted gross income of less than $9,000. U.S. Treasury Department, Internal Revenue Service, *Statistics of Income for 1960, Individual Income Tax Returns*, Table I, p. 32; U.S. Treasury Department, Internal Revenue

are a direct implementation of the Congressional concern that Section 117 should not exempt from taxation continuing salary payments to employees on leave from their regular jobs. There is neither a logical nor a legal basis for respondents' theory that Congress chose to exempt from tax all compensatory payments to degree candidates unless they were given in return for current services, as in *Reese* or *Woddail*, or fit the exact terms of Section 117(b)(1). Indeed, to exempt respondents' payments, while taxing the relatively modest amounts paid graduate teaching and research assistants as required under Section 117(b)(1) would reintroduce into the tax laws the very sort of inequity that Congress abolished when it limited the amount of exemption that could be claimed by nondegree candidates. (See our opening brief at pp. 12–16.) The Treasury Regulations are a rational and proper interpretation of the Congressional purpose [3] and the Third Circuit erred in refusing to apply them to this case.[4]

Service, *Statistics of Income for 1961, Individual Income Tax Returns*, Table I, p. 32; U.S. Treasury Department, Internal Revenue Service, *Statistics of Income for 1962, Individual Income Tax Returns*, Table I, p. 33.

[3] In their brief on the merits (p. 18), as in their brief in opposition to the petition, respondents seek to support their position on the ground that the Internal Revenue Service has under consideration revisions of the regulations under Section 117. As we pointed out in our reply to the brief in opposition, any substantive changes would allow the exemption on the facts of such cases as *Wells* v. *Commissioner*, 40 T.C. 40, see Rev. Rul. 65–59, 1965–1 Cum. Bull. 67, but not change the position taken in cases such as the present one.

[4] It does not follow from our position (see Respondents' Br. 10, 15) that all scholarships or fellowships would be taxable,

Respectfully submitted.

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FEBRUARY 1969.

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or that even all grants from employer to employee would fail to qualify for the exemption of Section 117. This case involves only the narrow problem of characterizing payments given in return for a promise to provide services or some other valuable consideration—a bartered transaction in which *quid pro quo's* are exchanged. Obviously this does not, as respondents would have it (Br. 7–9), encompass every grant given for the support of a scholar or researcher simply because the recipient promises to undertake studies or research. Of course, when the payment goes from employer to employee, a serious question will always arise as to the purpose of the arrangement. But if the money is not contingent on the promise of services—past, present or future—then it should qualify for the exemption.

U.S. GOVERNMENT PRINTING OFFICE: 1969

SUPREME COURT OF THE UNITED STATES

No. 473.—October Term, 1968.

John H. Bingler, District Director of Internal Revenue, Petitioner, v. Richard E. Johnson et al. } On Writ of Certiorari to the United States Court of Appeals for the Third Circuit.

[April 23, 1969.]

Mr. Justice Stewart delivered the opinion of the Court.

We are called upon in this case to examine for the first time § 117 of the Internal Revenue Code of 1954, which excludes from a taxpayer's gross income amounts received as "scholarships" and "fellowships." The question before us concerns the tax treatment of payments received by the respondents[1] from their employer, the Westinghouse Electric Corporation, while they were on "educational leave" from their jobs with Westinghouse.

During the period here in question the respondents held engineering positions at the Bettis Atomic Power Laboratory in Pittsburgh, Pennsylvania, which Westinghouse operates under a "cost-plus" contract with the Atomic Energy Commission. Their employment status enabled them to participate in what is known as the Westinghouse Bettis Fellowship and Doctoral Program. That program, designed both to attract new employees seeking further education and to give advanced training to persons already employed at Bettis, offers a two-phase schedule of subsidized postgraduate study in engineering, physics, or mathematics.

[1] We refer only to respondents Richard E. Johnson, Richard A. Wolfe, and Martin L. Pomerantz; their wives are parties to this action solely because joint tax returns were filed for the years in question.

Under the first, or "work-study" phase, a participating employee holds a regular job with Westinghouse and in addition pursues a course of study at either the University of Pittsburgh or Carnegie-Mellon University.[2] The employee is paid for a 40-hour work week, but may receive up to eight hours of "release time" per week for the purpose of attending classes.[3] "Tuition remuneration," as well as reimbursement for various incidental academic expenses, is provided by the company.[4]

When an employee has completed all preliminary requirements for his doctorate, he may apply for an educational leave of absence, which constitutes the second phase of the Fellowship Program. He must submit a proposed dissertation topic for approval by Westinghouse and the AEC. Approval is based, *inter alia*, on a determination that the topic has at least some general relevance to the work done at Bettis. If the leave of absence is secured, the employee devotes his full attention, for a period of at least several months,[5] to fulfilling his dissertation requirement. During this period he receives a "stipend" from Westinghouse, in an amount based on a specified percentage (ranging from 70% to 90%) of his prior salary plus "adders," depending upon the size of his family.[6] He also retains his seniority status and receives all employee benefits, such as insurance and stock option privileges. In return he must not only submit periodic progress reports, but under the written agreement that all participants in the program must sign, he is obligated to return to the employ of Westinghouse

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[2] Formerly Carnegie Institute of Technology.

[3] A maximum of 156 hours of release time per year is allowed.

[4] The Fellowship Program is funded jointly by Westinghouse and the AEC, but the amounts paid to participating employees are channeled through the company's payroll office.

[5] The ordinary leave period is nine months.

[6] Maximum monthly limits are placed on the amounts paid.

for a period of at least two years following completion of his leave.[7] Upon return he is, according to the agreement, to "assume duties commensurate with his education and experience," at a salary "commensurate with the duties assigned."

The respondents all took leaves under the Fellowship Program at varying times during the period 1961–1962,[8] and eventually received their doctoral degrees in engineering. Respondents Johnson and Pomerantz took leaves of nine months and were paid $5,670 each, representing 80% of their prior salaries at Westinghouse. Respondent Wolfe, whose leave lasted for a year, received $9,698.90, or 90% of his previous salary. Each returned to Westinghouse for the required period of time following his educational leave.

Westinghouse, which under its own accounting system listed the amounts paid to the respondents as "indirect labor" expenses, withheld federal income tax from those amounts.[9] The respondents filed claims for refund, contending that the payments they had received were "scholarships," and hence were excludable from income

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[7] Respondent Wolfe began his leave at a time when Westinghouse did not require agreement in writing to the two-year "return" commitment. He was formally advised before he went on leave, however, that he was "expected" to return to Westinghouse for a period of time equal to the duration of his leave, and he in fact honored that obligation.

[8] Respondent Wolfe was on leave from March 1, 1960, to February 28, 1961; respondent Johnson from October 1, 1960, to June 30, 1961; and respondent Pomerantz from November 1, 1961, to July 31, 1962.

[9] Tuition and incidental fees were also paid by Westinghouse, but no withholding was made from those payments, and their tax status is not at issue in this case. Although conceptually includable in income, such sums presumably would be offset by educational expense deductions. See Treas. Reg. § 1.162–5.

under § 117 of the Code, which provides in pertinent part:

"(a) *General Rule.*—In the case of an individual, gross income does not include—

"(1) any amount received—

"(A) as a scholarship at an educational institution (as defined in section 151 (e)(4)), or

"(B) as a fellowship grant . . . ."[10]

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[10] The entire section reads as follows:

"§ 117. Scholarships and fellowship grants.

"(a) General rule.

"In the case of an individual, gross income does not include—

"(1) any amount received—

"(A) as a scholarship at an educational institution (as defined in section 151 (e)(4)), or

"(B) as a fellowship grant, including the value of contributed services and accommodations; and

"(2) any amount received to cover expenses for—

"(A) travel,

"(B) research,

"(C) clerical help, or

"(D) equipment,

"which are incident to such a scholarship or to a fellowship grant, but only to the extent that the amount is so expended by the recipient.

"(b) Limitations.

"(1) Individuals who are candidates for degrees.

"In the case of an individual who is a candidate for a degree at an educational institution (as defined in section 151 (e)(4)), subsection (a) shall not apply to that portion of any amount received, which represents payment for teaching, research, or other services in the nature of part-time employment required as a condition to receiving the scholarship or the fellowship grant. If teaching, research, or other services are required of all candidates (whether or not recipients of scholarships or fellowship grants) for a particular degree as a condition to receiving such degree, such teaching, research, or other services shall not be regarded as part-time employment within the meaning of this paragraph.

"(2) Individuals who are not candidates for degrees.

"In the case of an individual who is not a candidate for a degree

When those claims were rejected, the respondents instituted this suit in the District Court for the Western District of Pennsylvania, against the District Director of Internal Revenue. After the basically undisputed evidence regarding the Bettis Program had been presented, the trial judge instructed the jury in accordance with Treas. Reg. § 1.117–4 (c), which provides that amounts representing "compensation for past, present, or future employment services," and amounts "paid . . . to . . . an individual to enable him to pursue studies or research primarily for the benefit of the grantor," are not exclud-

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at an educational institution (as defined in section 151 (e)(4)), subsection (a) shall apply only if the condition in subparagraph (A) is satisfied and then only within the limitations provided in subparagraph (B).

"(A) Conditions for exclusion.

"The grantor of the scholarship or fellowship grant is—

"(i) an organization described in section 501 (c)(3) which is exempt from tax under section 501 (a),

"(ii) a foreign government,

"(iii) an international organization, or a binational or multinational education and cultural foundation or commission created or continued pursuant to the Mutual Educational and Cultural Exchange Act of 1961, or

"(iv) the United States, or an instrumentality or agency thereof, or a State, a territory, or a possession of the United States, or any political subdivision thereof, or the District of Columbia.

"(B) Extent of exclusion.

"The amount of the scholarship or fellowship grant excluded under subsection (a)(1) in any taxable year shall be limited to an amount equal to $300 times the number of months for which the recipient received amounts under the scholarship or fellowship grant during such taxable year, except that no exclusion shall be allowed under subsection (a) after the recipient has been entitled to exclude under this section for a period of 36 months (whether or not consecutive) amounts received as a scholarship or fellowship grant while not a candidate for a degree at an educational institution (as defined in section 151 (a)(4))."

able as scholarships.[11] The jury found that the amounts received by the respondents were taxable income. Respondents then sought review in the Court of Appeals for the Third Circuit, and that court reversed, holding that the Regulation referred to was invalid, that the jury instructions were therefore improper, and that on the essentially undisputed facts it was clear as a matter of law that the amounts received by the respondents were "scholarships" excludable under § 117. 396 F. 2d 258.

The holding of the Court of Appeals with respect to Treas. Reg. § 1.117–4 (c) was contrary to the decisions of several other circuits—most notably, that of the Fifth

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[11] "§ 1.117–4. Items not considered as scholarships or fellowship grants

"The following payments or allowances shall not be considered to be amounts received as a scholarship or a fellowship grant for the purpose of section 117:

"(c) Amounts paid as compensation for services or primarily for the benefit of the grantor.

"(1) Except as provided in paragraph (a) of § 1.117–2, any amount paid or allowed to, or on behalf of, an individual to enable him to pursue studies or research, if such amount represents either compensation for past, present, or future employment services or represents payment for services which are subject to the direction or supervision of the grantor.

"(2) Any amount paid or allowed to, or on behalf of, an individual to enable him to pursue studies or research primarily for the benefit of the grantor. However, amounts paid or allowed to, or on behalf of, an individual to enable him to pursue studies or research are considered to be amounts received as a scholarship or fellowship grant for the purpose of section 117 if the primary purpose of the studies or research is to further the education and training of the recipient in his individual capacity and the amount provided by the grantor for such purpose does not represent compensation or payment for the services described in subparagraph (1) of this paragraph. Neither the fact that the recipient is required to furnish reports of his progress to the grantor, nor the fact that the results of his studies or research may be of some incidental benefit to the grantor shall, of itself, be considered to destroy the essential character of such amount as a scholarship or fellowship grant."

Circuit in *Ussery* v. *United States*, 296 F. 2d 582, which explicitly sustained the Regulation against attack and held amounts received under an arrangement quite similar to the Bettis Program to be taxable income.[12] Accordingly, upon the District Director's petition, we granted certiorari to resolve the conflict and to determine the proper scope of § 117 and Treas. Reg. § 1.117–4 (c) with respect to payments such as those involved here. 393 U. S. 949.

In holding invalid the Regulation that limits the definitions of "scholarship" and "fellowship" so as to exclude amounts received as "compensation," the Court of Appeals emphasized that the statute itself expressly adverts to certain situations in which funds received by students may be thought of as remuneration. After the basic rule excluding scholarship funds from gross income is set out in § 117 (a), for instance, subsection (b)(1) stipulates:

> "In the case of an individual who is a candidate for a degree at an educational institution . . . , subsection (a) shall not apply to that portion of any amount received which represents payment for teaching, research, or other services in the nature of part-time employment required as a condition to receiving the scholarship or the fellowship grant." [13]

In addition, subsection (b)(2) limits the exclusion from income with regard to nondegree candidates in two re-

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[12] Generally in accord with *Ussery* are *Reese* v. *Commissioner*, 373 F. 2d 742 (C. A. 4th Cir.); *Stewart* v. *United States*, 363 F. 2d 355 (C. A. 6th Cir.); and *Woddail* v. *Commissioner*, 321 F. 2d 721 (C. A. 10th Cir.). See also *Reiffen* v. *United States*, 376 F. 2d 883 (Ct. Cl.).

[13] Subsection (b) goes on to except from that limitation situations in which "teaching, research, or other services are required of all candidates (whether or not recipients of scholarships or fellowship grants) for a particular degree as a condition to receiving such degree . . . ." In those situations, scholarship or fellowship funds received for such services are nontaxable. See n. 10, *supra*.

spects: first, the grantor must be a governmental agency, an international organization, or an organization exempt from tax under §§ 501 (a), (c)(3) of the Code; and second, the maximum exclusion from income available to a nondegree candidate is $300 per month for not more than 36 months. Since these exceptions are expressly set out in the statute, the Court of Appeals, relying on the canon of construction that *expressio unius est exclusio alterius*, concluded that no additional restrictions may be put on the basic exclusion from income granted by subsection (a)—a conclusion forcefully pressed upon us by the respondents.

Congress' express reference to the limitations just referred to concededly lends some support to the respondents' position. The difficulty with that position, however, lies in its implicit assumption that those limitations are limitations on an exclusion of *all funds* received by students to support them during the course of their education. Section 117 provides, however, only that amounts received as "scholarships" or "fellowships" shall be excludable. And Congress never defined what it meant by the quoted terms. As the Tax Court has observed:

> "[A] proper reading of the statute requires that before the exclusion comes into play there must be a determination that the payment sought to be excluded has the normal characteristics associated with the term 'scholarship.'" *Elmer L. Reese, Jr.*, 45 T. C. 407, 413, aff'd, 373 F. 2d 742.

The regulation here in question represents an effort by the Commissioner to supply the definitions that Congress omitted.[14] And it is fundamental, of course, that as

[14] See also Treas. Reg. §§ 1.117–3 (a), (c), which sets out the "normal characteristics" associated with scholarships and fellowships:

"§ 1.117–3 Definitions

"(a) Scholarship. A scholarship generally means an amount paid or allowed to, or for the benefit of, a student, whether an under-

"contemporaneous constructions by those charged with administration of" the Code, the Regulations "must be sustained unless unreasonable and plainly inconsistent with the revenue statutes," and "should not be overruled except for weighty reasons." *Commissioner* v. *South Texas Lumber Co.*, 333 U. S. 496, 501. In this respect our statement last Term in *United States* v. *Correll*, 389 U. S. 299, bears emphasis:

> "[W]e do not sit as a committee of revision to perfect the administration of the tax laws. Congress

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graduate or a graduate, to aid such individual in pursuing his studies. The term includes the value of contributed services and accomodations (see paragraph (d) of this section) and the amount of tuition, matriculation, and other fees which are furnished or remitted to a student to aid him in pursuing his studies. The term also includes any amount received in the nature of a family allowance as a part of a scholarship. However, the term does not include any amount provided by an individual to aid a relative, friend, or other individual in pursuing his studies where the grantor is motivated by family or philanthropic considerations. If an educational institution maintains or participates in a plan whereby the tuition of a child of a faculty member of such institution is remitted by any other participating educational institution attended by such child, the amount of the tuition so remitted shall be considered to be an amount received as a scholarship.

"(c) Fellowship grant. A fellowship grant generally means an amount paid or allowed to, or for the benefit of, an individual to aid him in the pursuit of study or research. The term includes the value of contributed services and accommodations (see paragraph (d) of this section) and the amount of tuition, matriculation, and other fees which are furnished or remitted to an individual to aid him in the pursuit of study or research. The term also includes any amount received in the nature of a family allowance as a part of a fellowship grant. However, the term does not include any amount provided by an individual to aid a relative, friend, or other individual in the pursuit of study or research where the grantor is motivated by family or philanthropic considerations."

We are not concerned in this case with distinctions between the terms "scholarship" and "fellowship."

has delegated to the Commissioner, not to the courts, the task of prescribing 'all needful rules and regulations for the enforcement' of the Internal Revenue Code. 26 U. S. C. § 7805 (a). In this area of limitless factual variations, 'it is the province of Congress and the Commissioner, not the courts, to make the appropriate adjustments.'" *Id.*, at 306–307.

Here, the definitions supplied by the Regulation clearly are prima facie proper, comporting as they do with the ordinary understanding of "scholarships" and "fellowships" as relatively disinterested, "no-strings" educational grants, with no requirement of any substantial *quid pro quo* from the recipients.

The implication of the respondents' *expressio unius* reasoning is that any amount paid for the purpose of supporting one pursuing a program of study or scholarly research should be excludable from gross income as a "scholarship" so long as it does not fall within the specific limitations of § 117 (b). Pay received by a $30,000 per year engineer or executive on a leave of absence would, according to that reasoning, be excludable as long as the leave was granted so that the individual could perform work required for a doctoral degree. This result presumably would not be altered by the fact that the employee might be performing, in satisfaction of his degree requirements, precisely the same work which he was doing for his employer prior to his leave and which he would be doing after his return to "employment"—or by the fact that the fruits of that work were made directly available to and exploited by the employer. Such a result would be anomalous indeed, especially in view of the fact that under § 117 the comparatively modest sums received by part-time teaching assistants are clearly subject to taxation.[15] Particularly in light of the prin-

[15] Cf. 1 J. Mertens, Law of Income Taxation, § 7.42, at 110 (Zimet & Oliver rev. ed. 1962).

ciple that exemptions from taxation are to be construed narrowly,[16] we decline to assume that Congress intended to sanction—indeed, as the respondents would have it, to compel—such an inequitable situation.[17]

The legislative history underlying § 117 is, as the Court of Appeals recognized, "far from clear." [18] We do not believe, however, that it precludes, as "plainly inconsistent" with the statute, a definition of "scholarship" that excludes from the reach of that term amounts received as compensation for services performed. The 1939 Internal Revenue Code, like predecessor Codes, contained no specific provision dealing with scholarship grants. Whether such grants were includable in gross income depended simply upon whether they fell within the broad provision excluding from income amounts received as "gifts." [19] Thus case-by-case determinations regarding grantors' motives were necessary. The cases decided under this approach prior to 1954 generally involved two types of financial assistance: grants to research or teaching assistants—graduate students who perform research or teaching services in return for their stipends—and foundation grants to post-doctoral researchers. In cases decided shortly before the 1954 Code was enacted, the Tax Court, relying on the "gift" approach to scholarships and fellowships, held that amounts received by a research assistant were taxable

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[16] See *Commissioner* v. *Jacobson*, 336 U. S. 28, 48–49; *Helvering* v. *Northwest Steel Rolling Mills, Inc.*, 311 U. S. 46, 49.

[17] The opinion of the Court of Appeals reiterates that the stipends received by the respondents were "reasonable." Those payments approximated, of course, the respondents' previous engineering salaries. In any event, given the court's *expressio unius* reasoning, the source of a limitation based on the "reasonableness" of amounts granted to bona fide students is difficult to identify.

[18] 396 F. 2d, at 263.

[19] Int. Rev. Code of 1939, c. 1, § 22 (b) (3), 53 Stat. 10; see Int. Rev. Code of 1954, § 102.

income,[20] but reached divergent results in situations involving grants to post-doctoral researchers.[21]

In enacting § 117 of the 1954 Code, Congress indicated that it wished to eliminate the necessity for reliance on "case-by-case" determinations with respect to whether "scholarships" and "fellowships" were excludable as "gifts." Upon this premise the respondents hinge their argument that Congress laid down a standard under which all case-by-case determinations—such as those that may be made under Treas. Reg. § 1.117–4 (c)—are unnecessary and improper. We have already indicated, however, our reluctance to believe that § 117 was designed to exclude from taxation all amounts, no matter how large or from what source, that are given for the support of one who happens to be a student. The sounder inference is that Congress was merely "recogni[zing] that scholarships and fellowships are sufficiently unique . . . to merit [tax] treatment separate from that accorded gifts,"[22] and attempting to provide that grants falling within those categories should be treated consistently—as in some instances, under the generic provisions of the 1939 Code, they arguably had not been. Delineation of the precise contours of those categories was left to the Commissioner.

Furthermore, a congressional intention that not all grants received by students were necessarily to be "scholarships" may reasonably be inferred from the legislative history. In explaining the basis for its version of § 117 (b)(2),[23] the House Ways and Means Committee stated

[20] See, *e. g.*, *Banks* v. *Commissioner*, 17 T. C. 1386.

[21] Compare *Ti Li Loo* v. *Commissioner*, 22 T. C. 220 (university grant for National Health Service research held taxable), with *Stone* v. *Commissioner*, 23 T. C. 254 (foundation grant held nontaxable).

[22] Gordon, Scholarship and Fellowship Grants as Income: A Search for Treasury Policy, 1960 Wash. U. L. Q. 144, 151.

[23] That version provided for the exclusion only of grants that, together with compensation received from the recipient's former

that its purpose was to "tax those grants which are in effect merely payments of a salary during a period while the recipient is on leave from his regular job."[24] This comment related, it is true, to a specific exception to the exclusion from income set out in subsection (a). But, in view of the fact that the statute left open the definitions of "scholarship" and "fellowship," it is not unreasonable to conclude that in adding subsection (b) to the statute Congress was merely dealing explicitly with those problems that had come explicitly to its attention—*viz.*, those involving research and teaching assistantships and post-doctoral research grants—without intending to forbid application to similar situations of the general principle underlying its treatment of those problems. One may justifiably suppose that the Congress that taxed funds received by "part-time" teaching assistants, presumably on the ground that the amounts received by such persons really represented compensation for services performed,[25] would also deem proper a definition of "scholarship" under which comparable sorts of compensation—which often, as in the present case, are significantly greater in amount—are likewise taxable.[26]

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employer, were less than 75% of his salary for the preceding year. Noting that the House bill would have taxed many modest grants simply because the recipient had no substantial earned income in the previous year, the Senate rejected that formulation and substituted the present $300 per month, 36-month provision of § 117 (b) (2). See H. R. Rep. No. 1337, 83d Cong., 2d Sess., 17; S. Rep. No. 1622, 83d Cong., 2d Sess., 18.

[24] H. R. Rep. No. 1337, *supra*, at 17.

[25] The House version of § 117 (b) (1) taxed only amounts received as payment for teaching and research services. The Senate amended the provision, however, to include payments for "other services" as well. See S. Rep. No. 1622, *supra*, at 18.

[26] In connection with the question of what Congress may have intended to denote by the terms "scholarship" and "fellowship," it is noteworthy that the House Report stated, "Such grants gen-

In providing such a definition, the Commissioner has permissibly implemented an underlying congressional concern.[27] We cannot say that the provision of Treas. Reg. § 1.117–4 (c) that taxes amounts received as "compensation" is "unreasonable or plainly inconsistent with the . . . statut[e]." [28]

Under that provision, as set out in the trial court's instructions,[29] the jury here properly found that the

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erally are of small amount and are usually received by individuals who would have little or no tax liability in any case." H. R. Rep. No. 1337, *supra*, at 17.

[27] The Court of Appeals viewed the "primary purpose" of § 117 as the "encourage[ment of] financial aid to education through tax relief." 396 F. 2d, at 262. But while some desire to aid scholarship students no doubt underlay enactment of the statute, that desire must be reconciled with an apparent congressional intent—manifested in the limitations set out in subsection (b)—to tax amounts that represent compensation for services performed. As the text makes clear, we cannot view the Commissioner's attempt to achieve that reconciliation as improper.

[28] The Court of Appeals seems to have recognized that in some circumstances the Commissioner's approach is justified. Its opinion stated:

"A significant commitment by the student in return for a grant would, of course, place that grant outside the category 'scholarship,' at least to the extent of the value of that commitment. For if the grantee had to barter for his stipend, giving full value for it, this arrangement would hardly serve the primary purpose of the § 117 exclusion: to encourage financial aid to education through tax relief." 396 F. 2d, at 262.

It is not clear how this position can be squared with the Court of Appeals' holding that Treas. Reg. § 1.117–4 (c) is invalid. In any event, as we suggest *infra*, we cannot agree with the conclusion of the Court of Appeals that the grants received by the respondents were not "bartered for."

[29] The instructions included, *inter alia*, the following passage:

"You are . . . instructed that, one, any amount of money paid to an individual to enable him to pursue studies or research, if such amount represents either compensation for past, present or future

amounts received by the respondents were taxable "compensation" rather than excludable "scholarships." [30] The employer-employee relationship involved is immediately

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employment services, or represents payment for services which are subject to the direction or supervision of the grantor, . . . is not a scholarship or fellowship under the tax laws.

"Two, any amount of money paid to an individual to enable him to pursue studies or research which studies or research are primarily for the benefit of the grantor is not a scholarship under the tax laws."

[30] We thus endorse the decisions of the Fifth and Sixth Circuits in *Ussery* v. *United States*, 296 F. 2d 582, and *Stewart* v. *United States*, 363 F. 2d 355. In *Ussery*, the Court of Appeals for the Fifth Circuit specifically upheld Treas. Reg. § 1.117–4 (c) and held taxable monthly payments received by an employee of the Mississippi Department of Public Welfare who had been given leave to secure a Master's Degree in social work. The taxpayer there received employee benefits while on leave, and was obligated to return to the department following completion of his studies. *Stewart* involved a similar arrangement under which an employee of the Tennessee Department of Public Welfare received monthly stipends and other benefits during an educational leave of absence but was required to return thereafter to her previous position. See *Reese* v. *Commissioner*, 373 F. 2d 742 (C. A. 4th Cir.), affirming 45 T. C. 407 (student-teacher); *Woddail* v. *Commissioner*, 321 F. 2d 721 (C. A. 10th Cir.) (resident physician; obligated to remain following part-time participation in training program); cf. *Reiffen* v. *United States*, 376 F. 2d 883 (Ct. Cl.) (relying solely on characterization of payments as "primarily for benefit of grantor"). Several Tax Court decisions point in the same direction, although treatment of various factual situations under § 117 has not been marked by a great deal of consistency. See generally Tabac, Scholarship and Fellowship Grants: An Administrative Merry-Go-Round, 46 Taxes 485 (1968).

The Commissioner has acquiesced in *Evans* v. *Commissioner*, 34 T. C. 720 (see 1965–1 Cum. Bull. 4), which allowed exclusion where, although the taxpayer was obligated to work for the grantor following completion of her studies, there had been no previous employment relationship. See Rev. Rul. 65–146, 1965–1 Cum. Bull. 66. We are informed by the Solicitor General, however, that the

suggestive, of course, as is the close relation between the respondents' prior salaries and the amount of their "stipends." In addition, employee benefits were continued. Topics were required to relate at least generally to the work of the Bettis Laboratory. Periodic work reports were to be submitted. And, most importantly, Westinghouse unquestionably extracted a *quid pro quo* for its grants. The respondents not only were required to hold positions with Westinghouse throughout the "work-study" phase of the program, but also were obligated to return to Westinghouse's employ for a substantial period of time after completion of their leave.[31] The thrust of the provision dealing with compensation is that bargained-for payments, given only as a *quo* in return

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Evans acquiescence will be modified. See also *Broniwitz* v. *Commissioner*, P-H 1968 TC Mem. Dec. ¶68,221 (Sept., 30, 1968) (requirement of summer employment with grantor; held excludable).

[31] The contract's provision that employees who avail themselves of educational leave will be assigned duties "commensurate with [their] education and experience," and compensated at rates "commensurate with" those duties, is hardly sufficient to avoid the clear inference that their grants are fully bargained for and in the nature of compensation. The program is featured in Westinghouse's recruiting efforts as a benefit attractive to many potential employees. Moreover, as suggested in the text, participation in the program undeniably means giving up the right to take more remunerative employment elsewhere for a considerable period of time. Had the company modified its program so that the amounts of the "fellowship" grants were spread over the years preceding and following the educational leave—as increments to the respondents' salary, set aside in a company-administered "educational fund"—there could be little doubt that those amounts would have represented compensation. We see no persuasive reason why a different tax result should be reached under Treas. Reg. § 1.117–4 (c) on the actual facts involved here. There is no merit in the respondents' oblique suggestion that payment for *present* services is somehow different, with respect to the question before us, from deferred or anticipatory payments.

for the *quid* of services rendered—whether past, present, or future—should not be excludable from income as "scholarship" funds.[32] That provision clearly covers this case.

Accordingly, the judgment of the Court of Appeals is reversed, and that of the District Court reinstated.

It is so ordered.

MR. JUSTICE DOUGLAS would affirm the judgment for the reasons stated by the Court of Appeals in 396 F. 2d 258.

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[32] We accept the suggestion in the Government's brief that the second paragraph of Treas. Reg. § 1.117–4 (c)—which excepts from the definition of "scholarship" any payments that are paid to an individual "to enable him to pursue studies or research primarily for the benefit of the grantor"—is merely an adjunct to the initial "compensation" provision:

"By this paragraph, the Treasury has supplemented the first in order to impose tax on bargained-for arrangements that do not create an employer-employee relation, as, for example, in the case of an independent contractor. But the general idea is the same: 'scholarship' or 'fellowship' does not include arrangements where the recipient receives money and in return provides a *quid pro quo*." Brief for petitioner, at 40.

The respondents point out that the Internal Revenue Service is considering possible revisions of the Regulations under § 117. The Solicitor General informs us, however, that although revisions might "conform the Regulations to the results reached" in such cases as *Wells* v. *Commissioner*, 40 T. C. 40, no changes are contemplated with respect to situations such as that involved here. Reply Brief for Petitioner in support of certiorari, at 3, n. 2; see Rev. Rul. 65–59, 1965–1 Cum. Bull. 67.